PENSIONS AND INSURANCE

STATEMENT OF THE COMMITTEE

The following statement is made for the information of members of the Association and others interested in the plan for insurance and annuities offered by the Teachers Insurance and Annuity Association of America. At the December meeting of the Association this Committee presented its report which was unanimously adopted by the Association. In this report it was recommended that the plan of insurance presented by the Teachers Insurance and Annuity Association of America be not approved by the Association on three grounds, which may be briefly re-stated as follows:

(1) That the policies of the Insurance Association were not participating;

(2) That by it no adequate provision was made for professorial representation on the board of the new insurance company;

(3) That there was substantial identity in the management of the new Insurance Association with that of the Carnegie Foundation and that this committee regarded it as contrary to the best interests of education and of university teachers in America that the Carnegie Foundation should unite its functions as critic and mentor of educational policies and institutions with the distribution of financial benefits to teachers and institutions and the control, even though indirectly, of the savings of university teachers.

Statements published by the Carnegie Foundation and statements made by its President and circulated by the representatives of the Teachers Insurance and Annuity Association of America, since the publication of our report, have given rise to some misunderstanding and confusion with respect to these three fundamental objections, which it is the purpose of this statement to remove.

As was anticipated by our last report it was subsequently proposed by the Carnegie Foundation that associated institutions should require all teachers and instructors not entitled to the benefits of the former pension plan of the Foundation to purchase annuities of the new insurance company, the teacher to contribute 5 per cent of his salary to this purpose and the institution with which he is associated to contribute a like amount. The announcement of

this plan was made too late for consideration in our last report but some of the more obvious objections to it were commented on in a supplementary statement prepared by the President of the Association and the chairman of this committee, and published in the January–February, 1919, BULLETIN of the Association. This committee approves and adopts that statement.

Fortunately the compulsory feature of the plan has been withdrawn by action of the Executive Committee of the Foundation. Teachers in associated institutions are not to be required to purchase annuities of the new insurance company but associated institutions, in order to enjoy the benefits of association with the Foundation are required to offer to teachers appointed since November, 1915, the privilege of purchasing annuities in the new insurance association, the institution contributing one-half of the cost of the annuity, its total contribution not exceeding 5 per cent of the teacher's salary. So far as we are advised, very few associated institutions have adopted this plan. In most institutions the proposal has been referred to faculty committees, and in every instance but one (the University of Pittsburgh), so far as this committee is now informed, the reports of these committees have been adverse to the adoption of the plan. Especially noteworthy and informing are the reports on this subject of Stanford, Harvard, Yale, Bryn Mawr, and Wisconsin.

The withdrawal by the Carnegie Foundation of the compulsory feature of the annuity plan, the very general dissatisfaction of college teachers with the plan of insurance offered by the new insurance company, and the fact that most commercial companies organized or doing business under the laws of New York have found it desirable to offer the participating form of policy, as well as the marked tendency of insurance companies to give their policyholders increased representation in the management of their affairs, encouraged this committee to hope that the trustees of the Insurance Association could be induced to modify the plan of insurance so that the company should offer a participating form of policy and that some definite plan for representation of teachers on the board of trustees of the insurance company might be adopted. This committee accordingly suggested that the President of this Association present the entire matter anew to the trustees of the Insurance Association with the request that they consider the desirability of modifying the plan in these particulars. This request was made to the trustees

in a letter of the President of this Association to President Pritchett of the Carnegie Foundation and of the new Insurance Association by letter of June 27. Attention is directed to this letter, to President Prichett's reply of July 27, and to President Lovejoy's rejoinder of August 29, all of which are elsewhere printed in this number of the BULLETIN of the Association. Comment on this correspondence at this time seems unnecessary except to say that the position taken by President Pritchett appears to postpone indefinitely the realization of the hope which we had entertained that the plan of insurance might be modified in the important particulars already enumerated and that the fullest co-operation between the new insurance company and this Association and other representative teachers' organizations might be established, so as to ensure the ultimate success of the plan.

There has lately been published by the Carnegie Foundation and widely circulated among the teaching profession a pamphlet, entitled "Some Misapprehensions Touching Life Insurance," in which attempt is made to answer various criticisms which have been directed toward the insurance plan. So far as this pamphlet deals with the criticisms of the plan heretofore made in the reports of this committee, the author of the pamphlet evidently labors under some "misapprehensions" touching insurance which members of this Association are invited to share. As an aid to more intelligent consideration of the subject we direct attention to the more important of these misapprehensions.

(1) From a perusal of pages 34–38 of this pamphlet one would gain the impression that the participating policy affords no substantial protection to the policyholder because he is not in a position to control the trustees of an insurance company in determining the amount of surplus which they may establish in addition to legal reserve and that consequently the participating policy imposes no legal obligation on the trustees to treat any particular portion of the surplus as divisible. At page 36 of the pamphlet it is stated, "It is not permitted under the law to promise in advance to distribute any 'divisible' surplus. But when such surplus has been accumulated it may distribute it either by dividends or in such other way as the law may permit," and at page 38 we are told, "While the stock company writing non-participating policies may not promise such distribution in advance, once the surplus is earned the question of its divisibility is the same whether the company be organized in

one way or in another." These statements represent with substantial accuracy the legal situation as it existed in New York prior to the New York insurance investigation, but they do not state the situation as it has existed since 1906. Section 83 of the New York Insurance Law, as amended in 1906 and at one later date, expressly provides that all domestic insurance companies (except stock life insurance companies transacting business exclusively on a non-mutual basis and issuing only non-participating policies) "shall provide in every policy issued on or after the first day of January, 1907, that the proportion of surplus accruing on said policy shall be ascertained and distributed annually and not otherwise. Upon the thirty-first day of December of each year, or as soon thereafter as may be practicable, every such corporation shall well and truly ascertain the surplus earned by such corporation during said year. After setting aside from such surplus such sums as may be required for the payment of authorized dividends upon the capital stock, if any, and such sums as may properly be held for account of existing deferred dividend policies and a contingency reserve not in excess of the amount prescribed in this article, every such corporation shall apportion the remaining surplus, equitably to all other policies entitled to share therein."

By section 87 of the same article of the New York Insurance Law also amended by the law of 1906, the amount of contingency surplus or reserve which New York life insurance corporations may accumulate is expressly limited to a certain definite percentage of the net value of its total insurance policies calculated according to the requirements detailed in section 84 of the insurance law. The amount of this percentage varies with the total net value of the insurance written by any particular company, being 20 per cent or $10,000, whichever is greater, when such net value is $100,000 or less and gradually diminishing to 7½ per cent when the total value of insurance written is $50,000,000 or more. This limitation was the result of a careful study of the problem by the New York insurance investigation. It is not unreasonable in amount and has been generally considered to afford a very real protection to policyholders who are prudent enough to insure with a company issuing participating policies.

It will thus be observed not only that the company writing participating policies is required to contract that it will distribute its "divisible surplus" but there are definite statutory limits to the

amount of contingency reserve or surplus which such companies may accumulate, and by issuing participating policies they are legally obligated to treat as divisible any surplus in excess of the authorized contingency reserve. These provisions of the New York Insurance Law have compelled life insurance companies which, before 1906, had accumulated enormous surpluses at the expense of their policyholders to distribute their future excess premiums among the policyholders, and have been an important factor with associated legislation in bringing about the mutualization of the large stock companies. Moreover, the fact that the right of the policyholder to participate in surplus is contractual, affords him complete protection against its impairment by amendment of the charter or by-laws of the company, by action of its stockholders or trustees, whereas the holder of the non-participating policy has no legal protection against amendment of the charter, making possible the use of the surplus, to which he has contributed, for the benefit of the stockholders or in the promotion of some enterprise (insurance or otherwise), based on some newly discovered social philosophy.

In short there is no basis for the assumption made in "Some Misapprehensions Touching Life Insurance" that the participating policy does not afford, under the New York law, a very real and reasonably definite protection to the policyholder with respect to the use of the surplus of the company in which he is insured. In our judgment the experience of insurance companies in general and of the Carnegie Foundation in particular make it abundantly clear that the participating policy combined with some real representation on the board of trustees of the Teachers Insurance Association is essential to safeguard properly the interests of its policyholders with respect to that large part of the potential value of an insurance policy which results from the surplus earnings of the company's invested funds.

(2) While the pamphlet above referred to nowhere explicitly so states, it is calculated to create the impression on the mind of the reader that there are serious legal or practical obstacles to the Teachers Insurance Association issuing participating policies. At pages 36 and 37 of the pamphlet the statement is made "By incorporation in its present form the Teachers Insurance and Annuity Association of America secured to its policyholders these great advantages:

"(a) Freedom from overhead cost which absorbs some 20 per cent of the premiums of policyholders.

"(b) Policies having no loading and issued at the lowest net rate, which the law will permit;

"(c) The opportunity to work out in the future a real participation of the policyholders in the government of the Association."

At page 37 the question is asked, "Was it in the interest of the future policyholder to forego these great advantages in order to put into his policy an agreement that it would share in any distribution of future surplus which the company determined to be divisible?"

In a communication to members of the committee, President Pritchett has stated that, "In framing the charter of the Association the incorporators sought to put into the charter the condition that any surplus arising in the operation of the Association should be returned to the policyholders in dividends. The Insurance Department decided that this could not legally be done but permitted a clause to be inserted that prohibited the stockholders of the corporation from using such surplus for their own profit."

We have already referred in this statement to the fact that section 83 of the New York Insurance Law expressly requires companies organized under the law of New York to issue only participating policies unless they are stock companies transacting business exclusively on the non-mutual basis and issuing only non-participating policies. We are in a position to say that the New York Insurance Department makes no ruling such as that indicated in the statement above quoted, but on the contrary it holds, and so advised the Teachers Insurance and Annuity Association that a stock company may write participating policies provided it make annual distribution of its surplus, if any, after making legal reserve and proper contingency reserve as authorized in section 87 of the law. Both mutual and stock insurance companies are now and have for many years been writing participating policies in New York on this basis. As the New York superintendent of insurance points out in his correspondence with the President of this Association, printed elsewhere in this number of the BULLETIN, under "ordinary conditions" the stock companies pursuant to the provisions in section 87 of the insurance law cannot pay expenses except out of assumed mortality gains and loadings contained in the premium and this would involve the loading of the premium of the participating policy with an amount sufficient to meet its current expenses.

That such a procedure would not increase the net cost of insurance to the holders of participating policies is capable of mathematical

demonstration. The net cost of insurance is determined by the rate of mortality and the cost of administration, neither of which are dependent upon the form of organization of the company writing the insurance or the form of the policy written, whether participating or non-participating. The Teachers Insurance Association pays no dividends, hence its only items of out-go are payments stipulated for by its policies and administration expenses. What remains after creating the legal reserve and any contingency reserve within the authorized legal limit is applicable to the reduction of premiums. The company has only three substantial sources of income: (a) premiums; (b) interest earned on funds derived from premiums; (c) interest earned on its million dollar endowment. This last item amounting to about $45,000 annually is alone peculiar to the Teachers Insurance Association as distinguished from the ordinary commercial company. That this item of income may be used in reduction of premiums in the form of "dividends" and that overhead expenses may be charged to and paid out of loading of premiums does not seem to be open to question. In confirmation of this view we refer to the opinion, printed elsewhere in this BULLETIN, of George Richards, Esq., of the New York Bar, the author of a standard treatise on insurance law and a recognized authority on the subject.

The condition, therefore, is not the "ordinary one" which exists upon the organization of a company to write participating insurance without endowment or surplus fund with which to begin business. The Teachers Insurance Association now has a surplus income assumed to be sufficient in amount to meet its current overhead expenses, which in the distribution of its surplus as dividends may be used as an offset to loading of premiums legally required to meet expenses. The net cost of insurance cannot be greater under one plan or the other. Under the participating plan the divisible surplus will be greater in proportion to the amount of loading of premiums and its excess cost would ultimately be returned to policy-holders. It may be added that a reasonable loading to meet expenses while not adding to the net cost of insurance would add to the security of the plan in the event that a large volume of insurance should be written and the annual income from endowment should not be sufficient to meet overhead charges.

A comparison is made on pages 46 and 47 of the pamphlet between the participating policy with loaded premium and the non-participat-

ing policy issued with net premium, showing that the former costs more than the latter during the early life of the policy. This comparison, however, is not applicable to the present situation and is entirely misleading because the comparison is made between two policies of a commercial insurance company and not between the participating and the non-participating policy issued by a company having one million dollars endowment and no agency expenses.

The statement is made at page 36 that by "incorporation in its present form the Teachers Insurance Association secured to its policyholders this great advantage: freedom from overhead costs which absorb 20 per cent of the premiums of policyholders." Obviously this advantage is not secured by the adoption of a charter authorizing the use of non-participating policies only. This freedom from overhead cost will be due to some extent to the income of endowment, to some extent also to the fact that the mortality rate of college teachers is less than in the case of risks accepted by commercial insurance companies, but principally because it is proposed to write insurance without the expense of agents, savings which will be equally available if the participating form of policy is issued. These three items of savings are not available to the commercial company which does not write group insurance and they should, therefore, materially reduce the net cost of insurance of the participating policy during the early years of the policy below that of the policy issued on the same basis by a commercial company. The loaded premium rate on a policy issued by the Teachers Insurance Association if competently managed would thus not only fall below the net rate at a much earlier date than in the case of policies issued by commercial companies but the average life of the policies issued by the Teachers Association would probably be longer.

It is not demonstrable that a net premium rate on policies issued by the Teachers Association is more favorable than a loaded premium on a participating policy and there is every probability that with competent management the loaded premium with a contractual right to policyholders of participation in the surplus will materially reduce the cost of insurance below the net premium rate, and that the net premium on the participating policy will fall below the fixed premium of the non-participating policy at a relatively early time in the life of the policy. In any event we deem it of greater importance that the right of policyholders to share in the surplus should be contractual than that teachers should be induced to entrust

their savings to a company not giving them such contractual right by the hope of saving a relatively small difference in the premium during the early years of the policy.

(3) The pamphlet above referred to is also calculated to encourage the misapprehension that the authority to write participating policies necessarily involves mutualization of the company. Such, however, is not the fact. While this committee is of the opinion that the organization of the Teachers Association as a mutual company is advisable and would be an effective method of lodging control of the company with its policyholders, who are a homogeneous and organized body, and would ensure equitable distribution of its surplus to its policyholders, nevertheless mutualization of the company has nothing to do with the writing of participating policies. A stock company may issue participating policies and when dividends are not paid to stockholders as in the case of the Teachers Association the financial result to policyholders given equally competent management is precisely the same whether the company be controlled by the policyholders or the stockholders.

(4) Relation of Teachers Insurance Association to the Carnegie Foundation.

While this subject receives several pages of discussion in the pamphlet referred to, in which stress is laid on the fact that the two organizations are distinct corporations, it is not denied, nor can it be denied that their control is substantially identical. This statement constitutes no reflection on the personnel of their respective boards, but it does give emphasis to the fundamental unsoundness of the alliance of two organizations performing functions which in the interests of sound educational policy should never be brought under a single control, the one being a control of the finances of teachers, the other a supervisory relation over the educational policies of educational institutions which at the same time receive financial benefits from it.

Some intimation of the possible practical consequences of this alliance was given when the Foundation made the announcement (subsequently withdrawn) that associated institutions would lose the benefit of association with the Foundation unless they compelled their teachers to join with them in contributing to the purchase of annuities from the Teachers Insurance and Annuity Association, a "distinct and separate corporation."

It has lately come to our attention that one of the arguments

used to induce the governing board of an associated institution, whose pension system had been taken over by the Foundation, to accept the present non-compulsory plan for the purchase of annuities of the Teachers Association was that unless the institution did so it would be obliged to assume payment to its retired teachers of the pensions which were then being paid by the Carnegie Foundation. Whether the Foundation has actually taken that attitude, we are unable to say, but that it is in a position to take it and that associated institutions are without legal protection from such arbitrary action is not open to question. That any single man or group of men, however wise and conscientious, should be in a position to dictate the policy of educational institutions for whose control they are not legally responsible, through their power to continue or withhold financial largess on which such institutions have come to depend in time of financial stress, or through the control of the savings of their teachers, is a menace to the free development of education in the United States. The dangers of it may already be clearly discerned by those who are able to see beyond present financial advantage, promised but not contracted for by the Carnegie Foundation, to the ultimate consequences of yielding to the dictation of the Foundation in order that the promised benefit may not be withdrawn.

The joint commission appointed to consider the insurance plan evidently shared in this apprehension, since in its report it recommended the adoption of an elaborate scheme for the independent control of the insurance company. President Pritchett joined in this report and it was afterward approved by the trustees of the Foundation. The plan was subsequently abandoned on the organization of the Insurance Association, without explanation and for reasons which can only be surmised. In view of the charge made in "Some Misapprehensions Touching Life Insurance" and by President Pritchett in various published documents, of unworthy suspicions on the part of this committee, it may be said that if the position of this committee with respect to the control of the Insurance Company is to be ascribed only to unworthy suspicions, those suspicions appear to have been shared by the Commission of which President Pritchett was a member and in whose recommendations he concurred.

We have considered with care all available material which has been published or communicated to us with respect to the subject

matter of our previous report, including the correspondence which is published herewith and to which attention is especially invited, including also some correspondence of the chairman of this committee with the New York Insurance Department which cannot be published in full as the Superintendent of Insurance withholds his consent to publication of his official letters of April 15, 1919, and April 25, 1919.

We see no occasion for modifying our conclusions and recommendations previously made. On the contrary, the character of the defense made of the objectionable features of the proposed insurance plan as exhibited in the pamphlet referred to, and the correspondence printed herewith, confirm and strengthen our conclusion that university teachers should not accept any arrangement affecting distribution of surplus insurance funds to which they contribute which is less secure than a contractual one. Until such contractual right on the part of policyholders is secured and a definite plan adopted whereby they may select representatives to participate in the management of the Company, the success of the Insurance Company and its relation with its policyholders are too uncertain and its advantages over those offered by commercial companies too dubious to justify college teachers in purchasing its policies in preference to those offered by commercial companies. It is well to remember that the Teachers Insurance Association is not in a position to offer any advantage which the commercial company writing group insurance, cannot offer except the benefit of the income of its endowment. This at current rates of interest will produce annual income of about $45,000. When the benefit of this sum is distributed among the number of policyholders which must be secured to insure the success of the plan, the financial advantage to the individual policyholder will be so small as to be negligible when compared with the volume and money cost of teachers' insurance, an advantage which will not compensate for the failure to provide adequate protection for its policyholders in the distribution of surplus.

We are not without hope, based on the history of the principal insurance companies of the country, that the Teachers Insurance Association may ultimately find it advantageous to meet these conditions and ensure the success of the company by thus enlisting the support and co-operation of this and other teachers' organizations.

The Committee:

THOMAS S. ADAMS, Yale University
WALTER W. COOK, Yale University
F. S. DEIBLER, Northwestern University
FRANK H. DIXON, Princeton University
THOMAS C. ESTY, Amherst College
W. F. GEPHART, Washington University
JOHN H. GRAY, University of Minnesota
HENRY B. GARDINER, Brown University
M. W. HASKELL, University of California
OTTO HELLER, Washington University
JACOB H. HOLLANDER, The Johns Hopkins University
S. S. HUEBNER, University of Pennsylvania
JOSEPH JASTROW, University of Wisconsin
E. W. KEMMERER, Princeton University
ALFRED C. LANE, Tufts College
ARTHUR O. LOVEJOY, The Johns Hopkins University
H. A. MILLIS, University of Chicago
H. L. RIETZ, Iowa University
ASHLEY H. THORNDIKE, Columbia University
HENRY S. WHITE, Vassar College
W. F. WILLCOX, Cornell University
HARLAN F. STONE, *Chairman*, Columbia University

CORRESPONDENCE

I. CORRESPONDENCE WITH THE PRESIDENT OF THE TEACHERS INSURANCE AND ANNUITY ASSOCIATION

The following correspondence, growing out of the report of Committee P submitted at the last annual meeting and printed in the January BULLETIN, is published for the information of members.

1. Chairman Stone to President Pritchett

March 7, 1919.

Dear President Pritchett:

In your recent correspondence with Professor Rietz you intimated that I realize that the New York Statute is mandatory in requiring the organization of the Teachers Insurance and Annuity Association of America on the non-participating basis. In making such a suggestion I am sure you are under some misapprehension, as I have never had any doubt but what it would have been possible and desirable to organize the insurance company on the participating basis. This

could have been accomplished by organizing the company as a mutual company since being an endowed company the ordinary financial difficulties of organizing a mutual company in New York would not have existed. It could also have been accomplished by abandoning the net rate program and raising the premium rate sufficiently to meet the requirements of the insurance department, giving to the policy-holders a contractual right to the distributable surplus as earned. There are, I believe, other ways.

In your interview in the *New York Evening Post* of March 6 you state, "The report of the Committee of the Association of University Professors recently published contains, unfortunately, a number of errors as to the facts and various misapprehensions based on lack of technical familiarity with technical questions of insurance and with the requirements of the New York law." The members of the Committee on Pensions and Insurance would very much appreciate it if you would state specifically what are the errors and misapprehensions to which you refer.

We would also appreciate your assistance very much if you would state specifically the errors and omissions in Mr. Linton's recent article to which you refer in your letter to me of February 21. I take pleasure in enclosing herewith for your information copy of a letter which I have just sent to the members of the Committee, with reference to your recent communication to certain members of the Committee. I am much gratified to learn that the plan for compulsory annuities has been withdrawn.

Yours sincerely,

HARLAN F. STONE.

2. President Pritchett to Chairman Stone

March 26, 1919.

My dear Dean Stone:

Absence, illness and a great pressure of work have prevented an earlier reply to your letter of March 7th, asking me to indicate the misapprehensions contained in the report of your Committee on the Teachers' Insurance and Annuity Association, referred to when I declined to discuss with a reporter Professor Lovejoy's interview.

The circulation of the pamphlet of the Provident Life and Trust Company among teachers has made an occasion for preparing a statement setting forth not only the misleading character of this pamphlet but also the principal matters concerning which there seems to have been some confusion of mind—mutualization, non-participating policies and the advantages to the policy holder of a company freed from overhead charge. This will be sent you as soon as it is in print. Since the poor professor who thinks of taking a policy in the Teachers' Association has to run the gauntlet of the Provident Life, the Professors' Association and Professor Cattell, it seems only fair to give him a chance for his life.

These matters are the fundamental ones concerning which your report seems to me to leave an unfortunate impression on the teacher. There are various other matters of minor importance—such as the omission of a million dollars in stating the reserve fund—which it is not necessary to go into.

So far as the misstatements in your report concern the Carnegie Foundation, it

does not seem to me wise to undertake to reply to them. We have not attempted to reply to such statements in the past and to do so now would involve me in a fruitless discussion, to which some members of your Committee are much addicted.

The fundamental objection to your reports (aside from the casual way in which they are put together) seems to me to lie in the spirit and temper in which they were made. You began with the charge that the contributory plan was "a suggested change in the fundamental purpose of the Foundation under the guise of a change of rules" and this attitude runs throughout the reports. For example in your last report, it is this spirit which prompts the charge that the Carnegie Foundation is seeking to control the Teachers' Association for ulterior purposes. Only in such an attitude of mind would your Committee have made the erroneous statement that "of the trustees of the Insurance Company, eight are or recently have been trustees or employees of the Carnegie Foundation." The facts are four trustees of the Foundation are trustees of the Insurance Association; two men associated with the Foundation served temporarily in order that the charter might be accepted. This fact was fully known to you and is referred to elsewhere in your report. When you declined to take one of these places it was filled by Professor Glover of Michigan, the chairman of the Committee of the Institute of Actuaries, which reported on the plan of the Association. The other two places to which you refer as filled by "trustees or employees" exist only in imagination. Professor Nicolson—whom you name as one of them—never had anything whatever to do with the Foundation. I never saw him until he came to the organization meeting of the trustees of the Teachers' Association. This sort of erroneous statement is the reflection of that sort of suspicion that inevitably obscures judgment—the one will make the other impossible.

Just why your Committee should be concerned that four of the trustees of the Foundation are also trustees of the Association is difficult to understand. Three of them are business men and especially qualified for service as Trustees of such a company. Two of these are among the ablest and best known financial men of the country. I really do not think they have been contaminated by this membership in the Board of Trustees of the Foundation.

So far as I am personally concerned I became president of the Insurance Company because for the first few years that officer must do a lot of work, the overhead of the Association needs to be kept down and I had no other way of getting the work done without paying a large salary except to do it myself. If some one else will take it on the same terms, I shall be delighted. The sort of suspicions voiced in these and similar accusations, thrown without discrimination into such a report, seems to me out of place among highminded and scholarly men.

The question of a sound plan for the protection of the teacher against the two principal hazards due to his economic situation is a matter of very great importance to the teachers of the next generation. All but three or four of the members of your large Committee will receive retiring allowances through the Carnegie Foundation and have in the decision of the question no such interest as younger teachers. For this reason there would seem to be all the greater reason for dealing with this important matter without prejudice or feeling. It is a singular part of the situation that your Committee should conduct an active propaganda against the Teachers Association. It is still more anomalous that a committee which felt itself competent to advise in so complicated a matter as the incorpora-

tion of an insurance company under the New York laws should lend itself to the circulation of a pamphlet like that of Mr. Linton's whose fallacies ought to be patent to any one familiar with the matter of endowment policies. I know you have been extremely busy with your various duties during the last year but it seems to me no less a misfortune to your Committee than to the younger teachers that you should not have found the time to take up completely and fully the reasons which have brought about the present organization of the Teachers' Association. I wonder if you will be good enough to send a copy of this to the members of your Committee?

Yours sincerely,

HENRY S. PRITCHETT.

3. *Chairman Stone to President Pritchett*

April 3, 1919.

My dear President Pritchett:

I have your letter of the 26th in reply to my letter of the 7th. As is my custom, I shall take pleasure in transmitting copies of your letter to the members of the Committee on Pensions and Insurance, together with a copy of this reply.

It would be easy to indulge in a prolonged discussion and controversy over what appear to me to be the immaterial and irrelevant matters to which your letter refers. But it does not seem to me that it would be profitable to do so, either from the point of view of the Teachers Insurance and Annuity Association or of the Committee on Pensions and Insurance. The last report of the Committee on Pensions and Insurance made four points with respect to the insurance plan of the Teachers Insurance and Annuity Association:

(1) That taken as a whole the policies offered by the Teachers Association, so far as they were legal obligations of the Association, did not offer to teachers any advantages over policies offered by the better class of commercial insurance companies. In some respects the policies of the Teachers Association were not as satisfactory as those offered by commercial companies.

(2) That no definite plan was offered for policy-holders' representation on the Board of Trustees of the Insurance Company.

(3) That the policies were not participating.

(4) That the Insurance Company was for all practical purposes under the control of the Carnegie Foundation. It was not charged, as you state in your letter, that the Carnegie Foundation "is seeking to control the Teachers Association for ulterior purposes," but it was stated in this and a previous report of the Committee, adopted by the American Association of University Professors, that it was deemed undesirable, as a matter of principle, that the control of the savings of teachers should be vested, directly or indirectly, in a body assuming to exercise a supervisory relation to American colleges and universities. The report of the Joint Commission which you signed and which was approved by the Carnegie Foundation seems to be based on a similar opinion, as the report favored the adoption of an elaborate scheme for independent control of the Insurance Company.

Some comment was also made in our report on the undesirability of the compulsory annuity plan, but as this plan has now been abandoned by the Carnegie Foundation further consideration need not be given to it.

I have read your letter very attentively and I confess that I do not find anything in it impairing in any way the validity of these conclusions. The only question of fact which you raise with respect to our report which appears to have any applicability is whether the statement contained in the report that "of the trustees of the Insurance Company, of which six constitute a quorum, eight are or recently have been trustees or employees of the Carnegie Foundation" should not have read "seven" instead of "eight." For although you refer to two of the "places" being filled with "trustees or employees," as "existing only in imagination," I assume that you do not intend to deny that in addition to four trustees of the Foundation who are trustees of the Insurance Association there were at the time of our report three other trustees of the Insurance Association who were or had lately been in the employment of the Foundation. What is more to the point, it cannot be denied that for all practical purposes there is substantial identity in the control of the Foundation and of the Insurance Association. In short the error which you mention in the reference to Professor Nicolson, and which was due to the misinformation of a member of our Committee, while regrettable, was in matter of substance immaterial. If this is the most pertinent criticism which can be made in point of fact about the report of the Committee, the Committee is to be congratulated on its success in pointing out to the teachers of the country the fundamental weaknesses of the plan of insurance presented for their consideration and acceptance by the Carnegie Foundation and the Teachers Insurance and Annuity Association of America. The report is courteous in tone, and it seems to me could give offense only in so far as the facts which it states are embarrassing or annoying.

In the interest of accuracy may I again say, as stated in my letter of March 7, in reply to your inquiry, that the Committee on Pensions and Insurance is not in any way responsible for the circulation of Mr. Linton's pamphlet. At the request of a member of the Committee I assisted him in procuring a list of the members of our Association which he gave to Mr. Linton for use as a mailing list. I should be very glad to extend a like courtesy to you or to any other person desiring to communicate with members of the Association. I may say, further, that the notion that any question can be properly settled by suppressing discussion of it is not one held by our Committee; and while the matter is one which has never been considered or acted on by it, I have no doubt that it will be very glad to have the points made by Mr. Linton in his pamphlet thoroughly considered and discussed by college teachers of this country.

May I also call attention to the fact that the suggestion in your letter that our report omitted to state the reserve fund of the Insurance Company as one million dollars is based on a misapprehension. The statement contained in our report at page 8 that the Insurance Company has a capital stock of $500,000 and that one million dollars has been paid in with which the Company is to begin business seems to conform to the financial statement of the Insurance Company published at page 1 of the Insurance Hand-Book.

While I am, as you say, a busy man, a large part of my time during the past year, as you know, has been devoted to the effort to secure such co-operation between the Committee of which I am a member, and the Carnegie Foundation as would bring about a satisfactory solution of the insurance problem. I do not believe that I am wholly ignorant of the reasons which have brought about the

present organization of the Insurance Association. Those reasons are, I think, patent to every one familiar with the situation. What I do not understand is why those efforts have met with so little response on your part and why in the effort to solve the problem a plan was adopted embodying such fundamental weaknesses as our report points out, and why it was adopted despite the protests of the teachers of the country whose interest and co-operation it will be necessary to secure in order to make the plan a success. I sincerely hope that this unfortunate situation may yet be corrected.

Yours sincerely,

HARLAN F. STONE.

4. *President Lovejoy to President Pritchett*

June 27, 1919.

My dear President Pritchett:

The recent correspondence between yourself and Dean Stone, of which he has sent me copies, seems to me to leave in a somewhat unsatisfactory state the relations between this Association and the Teachers Annuity and Insurance Association. The natural relation between the two bodies, in view of their purposes and reason for being, is one of co-operation. The Association of University Professors, as I need hardly say, earnestly desires to see a sound and secure system of insurance and annuities for college and university teachers established. Its officers are, and have at all times been, ready to co-operate with any other organization to that end; and they cordially welcomed the announcement of the purpose of the Carnegie Foundation to make special provision for furnishing insurance to teachers upon advantageous terms. It is still our desire to render any assistance in our power towards the realization of the announced objects of Mr. Carnegie's benefactions for the advancement of the teaching profession, and to promote the specific objects of the Insurance Company recently created by the Carnegie Corporation. It is, then, in the hope of aiding to bring about a co-operation between the two associations which may further the purpose common to both, that I am now writing you.

The officers of this Association and its Committee on Pensions and Insurance naturally cannot recommend to the members any insurance scheme which they believe to contain seriously unsatisfactory features. The report of the Committee with the Supplementary Statement, published in January, pointed out several such features in the methods of organization of the Teachers Insurance and Annuity Association, and in the proposed types of policy and rates of insurance, as these were stated in the Hand-Book and in the Carnegie Foundation's circular of December 6, 1918. We have been happy to learn that one of the provisions to which especial objection was made in the Supplementary Statement has been abandoned by the action of the Executive Committee of the Carnegie Foundation on February 26, 1919. We are thereby encouraged to hope that, after further study of the problem and fuller acquaintance with the views of the teachers and institutions affected, the trustees of the Insurance and Annuity Association may be disposed to reconsider the remaining features of the original plan to which exception has been taken—features which we believe to be unacceptable to the great majority of college and university teachers. Permit me, therefore, to recall the principal points in question:

1. Non-participating Policies

If the new company should write any large amount of insurance, it should, within a few years, at the present rates of premium and with its especially good class of risks, accumulate a considerable surplus. This surplus will consist largely of interest accruing on sums paid by college teachers out of their savings. Under the policies now offered, these teachers will have absolutely no contractual or other legal assurance that this surplus, resulting from their own contributions, will be returned to them, either in the form of dividends or of reductions in premiums or of increased insurance. Further reflection will, I am sure, convince you and your associates of the Board of Trustees that this is a wholly undesirable arrangement, and that it is especially out of keeping with the purposes for which the new company was endowed. No man should—as was pointed out by yourself and the other members of the Joint Commission in 1917—"accept any arrangement less secure than a contractual one" in a matter of this kind.

We are the more hopeful of your reconsideration of this matter because it appears that the original decision to offer only non-participating policies was reached under a misapprehension. Statements made by you since the publication of the report of the Committee of this Association, indicate that it was your belief, and that of the incorporators of the new company, that it is virtually impossible to establish a new participating company under the insurance laws of the State of New York—at least in such a way as to make the interest on the endowment, in the case of an endowed company, available for the benefit of the policy-holders. We have, however, obtained opinions concerning this point from competent legal advisers, from insurance experts, and from the Superintendent of Insurance of the State of New York; and we are convinced that there are no insuperable legal obstacles to the establishment of a participating company in that state, or to the conversion of the Teachers Insurance and Annuity Association into such a company, by amendment of its charter.

It is, indeed, true that, if organized on the participating plan, the company would, in order to conform to the law, be compelled to pay its running expenses out of premiums received, not, as now, out of the interest on the endowment; and that this, especially at the outset, would probably make it necessary to fix the premiums at a higher rate than at present. But this would mean no real increase in the annual cost of insurance to the policy-holders in this company; for the additional loading of the premiums could very simply be offset by the payment to the policy-holder of a corresponding amount out of the earnings of the company's initial capital given it by the Carnegie Corporation.

The change required, in short, would be little more than a matter of book-keeping; yet by this change it would become possible to give the policy-holder legal assurance of participation in the surplus earnings on the payments made by him. There clearly would be no legal difficulty in the above suggested use of the interest on the company's capital, if the company were a participating one. In reply to a specific question on this point, the Superintendent of Insurance of the State of New York writes: "I do not know of any provision of the law which would prohibit a company operating on the participating plan from distributing the earnings on its capital stock and surplus to its policy-holders in the form of dividends."

2. Organization of the Company

The new company has, we assume, been established in the interest of teachers. Its success and usefulness will depend in no small measure upon the degree of confidence which the members of the university teaching profession have in it. One of the most important means of creating and maintaining such confidence lies in giving to the body of teachers at least an equal representation in the governing board of the company, and in its responsible committees. Such representation is obviously no more than equitable, since, if the company realizes its purposes, by far the greater part of the funds will within a short time be contributed by the policy-holders and will be essentially their property. Unless some arrangement be made for the effectual participation of policy-holders in the control of the company, either by eventual mutualization, or by such a plan as was

recommended by the Joint Commission in 1917, it cannot be expected that the new company will appeal to most college or university teachers in any greater degree than do numerous existing companies, or that it will seem to them to be what its name implies, a *Teachers'* Insurance and Annuity Association.

In this connection, I quote an opinion given us by a member of the New York Bar (not connected with this Association), an eminent authority on the law of insurance. Referring to the remedial legislation of 1906, consequent upon the Hughes investigation, he writes: "A conspicuous purpose of this legislation was to give to policy-holders a more effective voice in the government of the companies and to compel the companies to make equitable distribution of surplus to the policy-holders at stated periods. This last-named provision of the statute is now embodied in Section 83 of our present Insurance Law, but by its express terms it is not applicable 'to any stock life insurance corporation which . . . shall transact and shall represent itself as transacting its business exclusively upon a non-mutual basis and shall . . . issue only non-participating policies.'

"By making the policies non-participating, then, it would appear that the policy-holders are to be put back into the predicament in which they found themselves before this remedial legislation was enacted. I would not consent to it for one moment. I agree with you and your committee wholly. The assets, the benefits whatever they are, must essentially belong to the policy-holders and to no one else. . . .

"If it is possible to arrange for a mutual company, I agree with you that that form of organization would best fit the case. Judge Marshall has recently given a pertinent description, in an important litigation, of the essential nature of a mutual company:

"As regards rights and remedies, the policy-holders are the stockholders. While the title to the property is in the company, the equitable interests therein are vested in the members. For all except corporate purposes the property of a mutual insurance company belongs to its members.' (*Huber* v. *Martin*, 127 Wis. 412.)

"Likewise, the Kentucky court has recently declared that the surplus of a mutual company belongs to the policy-holders. (*U. S. Life Ins. Co.* v. *Spinks*, 126 Ky. 405.)"

There are, no doubt, certain familiar objections to mutual companies; but these objections apply chiefly to the attempt to carry out the idea of mutuality in the case of companies whose policy-holders are too numerous, too heterogeneous and too unorganized to be capable of any intelligent action in common under ordinary circumstances. No such objections are pertinent in the case of a company serving a single profession of relatively small numbers—a profession, the members of which are presumed to possess a certain intelligence; which includes in its membership numerous experts in finance and economics, and not a few men who have had extensive administrative experience; many of whose members are organized into a single body; and which possesses various means for the formation, through discussion, of a collective judgment, and for its expression.

It is possible, however, that some other plan than that of mutualization might serve the same ends equally well. What seems, I am certain, to the great majority of this Association to be indispensable for the success of the new company is some arrangement whereby teachers are assured a much greater participation, through responsible representatives, in the direction of the company than is at present afforded them.

3. Special Features of Policies Offered

Several of the specific provisions of the policies now offered seem to our Committee on Pensions and Insurance to be susceptible of modification in ways which would render them both more useful and more attractive to potential purchasers. I shall not here dwell upon these suggested modifications in detail, as they have been sufficiently indicated on page 32 of the Committee's Report (January BULLETIN of this Association).

In making these suggestions for changes in certain of the present arrangements and regulations of the Teachers' Insurance and Annuity Association, our wish has

been to contribute to the success of the new enterprise and to the realization of the purposes for which it was established. The right of this Association to express itself upon a matter of this kind, or the appropriateness of its doing so, cannot, I take it, be seriously questioned. The membership of the Association does not, it is true, include all the college and university teachers in the United States. But it includes the great majority of teachers of the higher grades and of more than ten years' service, in all the larger or more important institutions. Its 2,300 members represent 143 institutions; and there are more than fifty organized local branches. A consensus of the opinions of members of the Association is, therefore, likely to be fairly indicative of the prevailing opinion of the professorate of the country; and certainly no other organization exists which is so nearly representative of the profession as a whole.

Upon no matter, I believe, has there ever been indicated a closer approach to unanimity of opinion and feeling, among the members of the Association, than upon those to which I have above referred. This fact I assume to be one of which it is desirable for the trustees of the Insurance and Annuity Association to be informed. And in view of the objects for which the new foundation exists, and of the importance of definite co-operation between it and the members of the profession for whose advancement it has been established, I venture to hope that the trustees of the Insurance and Annuity Association will, at the earliest convenient date, take up the question of a reconsideration of the features of the present plan to which reference has been made above. The Association of University Professors would be glad to send representatives to any meeting of your trustees which may be held for this purpose, to present our suggestions more fully and to consider possible methods of co-operative action.

I am sending copies of this letter to all the trustees of the Insurance and Annuity Association, and also to the trustees of the Carnegie Foundation. I shall be grateful for an early reply, which I shall, of course, wish to publish, together with this, in the BULLETIN of our Association. I am,

Very truly yours,

ARTHUR O. LOVEJOY.

5. President Pritchett to President Lovejoy

SANTA BARBARA, CALIF., July 27, 1919.

My dear Sir:

I beg to acknowledge your letter of June 27, which reached my office a few days after I had gone to the Northwest to attend a series of conferences, and which only recently came into my hands.

Your letter proposes a reorganization of the Teachers' Insurance and Annuity Association so as to make it a mutual company writing participating policies. I understand from your letter that in case this suggestion is carried out the Teachers Insurance Association may expect the approval of the American Association of University Professors.

The question of mutualization and of so-called participating policies was, as you know, most carefully considered in the organization of the Teachers Insurance Association. In determining the questions the best legal and actuarial aid was sought. It became entirely clear to those engaged in these examinations that

the interests of the future policy-holders—which was the sole end in view—would be best served by organizing the company in the form of a stock company. The reasons for this conclusion are fully set forth in the enclosed pamphlet, entitled "Some Misapprehensions Touching Life Insurance," which I hope may receive at your hands a careful examination.

Not only the question of mutualization of the Company but also that of the representation of policy-holders in its management is there fully discussed. The pamphlet contains in fact answers to all the questions raised in your letter.

I do not know the eminent authority on the law of insurance whose opinion you quote, but he is certainly wrong in stating that a conspicuous purpose of the 1906 legislation was to give to policy-holders (in general) the rights and privileges he specifies. The intention of Sections 83 and 97 was to correct certain defects which had been brought to light in the conduct of mutual companies only. *Their* policy-holders were to be protected on the one hand (Section 83) against the withholding or unfair distribution of the surplus rightfully belonging to them; on the other hand (Section 97) against the decrease of this same surplus of theirs by extravagant expenditures, particularly in connection with solicitation of new insurance. The question whether non-mutual companies should be mutualized was not affected and was not intended to be affected by either section. Hence the express and proper exemption of non-mutual companies.

Your suggestion that the premiums should be loaded so as to permit the issuance of participating policies, and that an amount corresponding to the loading should then be returned to the policy-holder out of interest on invested funds would constitute an evasion of the law that no responsible board of trustees would be willing to countenance. But even if this were done, there would still remain the problem of conducting the company within the amount furnished by loadings on policies which during the first years of the existence of a company would be wholly inadequate to bear the expenses of the most conservative business.

I venture to add that the Superintendent of Insurance of the State of New York has sent me a copy of his letter to you of May 31, in which he makes clear the fact that while the organization of a new company on the mutual plan is legally provided for it is nevertheless practically impossible and that it is equally impossible for a new life insurance company charging low premium rates to announce participation in dividends. In view of this official statement in your hands, the trustees of this Company find it difficult to understand upon what ground you still urge upon them the mutualization of the Teachers' Insurance and Annuity Association.

I note with pleasure your expression of willingness to co-operate with the officers of the Teachers' Insurance and Annuity Association. The officers and trustees of the Association have made every possible effort to co-operate with the college and university teachers of the United States and Canada and they will continue to do so. They have sought particularly to co-operate with the Committee of the American Association of University Professors. I asked of you both verbally and by letter the opportunity to lay before you the reasons which had led to the form of organization finally adopted and invited you to meet the experts who would set forth these reasons. To my regret you declined this invitation. Had you been willing to go over these matters in some such conference it seems to the trustees impossible that you could have failed to appreciate the reasons which prompted these experts to advise the present form of organization.

I note also with pleasure your statement as to the interest of the members of the American Association of University Professors in the matter of old age annuities and insurance and their desire to contribute to the success of the new enterprise for securing to college teachers the best facilities for protection against the hazards of dependence arising through premature death or old age or disability. In the determination of the principles and organization of the Teachers' Insurance Association, the trustees of the Foundation made every effort to consult with the Association of University Professors and to obtain their views and their co-operation, not as experts in insurance management, but as teachers directly interested in a solution of these problems and who, when they became policy-holders, ought to be represented in some effective way on the Board of Trustees by men chosen by them. No more cordial or appreciative welcome was given to the American Association of University Professors at its inauguration than by the Carnegie Foundation—Ninth Annual Report, pp. 59–61. The Foundation welcomed this new association as a promising agency in American education and one able to render a distinct service. The Foundation followed this expression of good will by a very practical step. It referred to the Association its provisional plan for a contractual and contributory pension system and invited criticism and discussion. The Committee on Pensions was appointed at the request of the Foundation. When this Committee desired additional time to consider the provisional plan, the trustees of the Foundation postponed for a year action on the provisional plan in order to give the Committee full time for its deliberations. It also invited the Association to name two members of the Joint Commission appointed to consider the provisional plan and these gentlemen joined in the unanimous report rendered by this Commission. If there is *any other thing* the trustees of the Foundation could have done to show a desire for friendly co-operation with the Association of University Professors they would gladly have done it.

The reports of your Committee have unfortunately been characterized by many misapprehensions arising out of the limited knowledge of its members touching technical details of insurance organization and management concerning which your Committee offered advice. The fundamental objections to the reports of the Committee lie, however, in the spirit and temper in which they have been made. The trustees of the Foundation have been represented in these reports as actuated by secondary and unworthy motives, and as seeking to evade their just obligations. Every effort has been made in these Reports to create an artificial antagonism between the members of the university who are in teaching positions and those in administrative positions. The trustees of the Teachers' Insurance Association would be slow to believe that these reports represented the spirit and temper of the 2,300 American scholars who make up the membership of the Association. The trustees have noted with regret that the meetings of the Association of University Professors bring together only a handful of its members. A very small group speaks in the name of the whole membership of the Association, a situation much to be regretted and one that goes far to take away its representative character.

The trustees of the Teachers' Insurance and Annuity Association are an entirely different body from the trustees of the Carnegie Foundation, notwithstanding the fact that the Teachers' Insurance Association grew out of the experience of the Foundation. They will gladly welcome co-operation with the

American Association of University Professors in the future. They regret that the Teachers' Insurance and Annuity Association should have met at your hands, hitherto, not friendly criticism but active hostility They particularly regret that the Association should have circulated among its members the statement put forth by the Provident Life and Trust Company in the endeavor to sell its own policies. The misleading character of this publication is fully set forth in the small pamphlet that is enclosed entitled, "Misapprehensions Touching Life Insurance." It is in the opinion of the trustees of the Teachers' Insurance Association to be regretted that an advertising effort of a commercial insurance company, entirely misleading in its character, should have been circulated through the agency of the American Association of University Professors and ostensibly with its approval.

I venture to suggest one other view of this matter which seems to me of significance to your Committee and to the Association itself. The members of your Committee with few exceptions are protected by old age pensions provided by the Carnegie Foundation. To carry out these payments during the next thirty or forty years a large reserve has been formed amounting to many millions of dollars. A very considerable proportion of the teachers in your Association are also protected by these pensions. Your younger colleagues now entering the profession of the teacher will not have this privilege. They are more fortunate in having available for their use an agency under which they may obtain old age annuities upon terms that are contractual, which are within the reach of the teacher's salary, and which afford him the widest degree of freedom. The plan rests upon those principles which alone can make a system of annuities permanent and feasible, alike to the teacher and his college.

Your Committee has sought to discourage younger teachers from availing themselves of the extraordinary facilities offered in the policies of the Teachers' Insurance Association. To accept on the one hand a retiring allowance full paid by the Carnegie Foundation and to seek to prevent at the same time younger teachers not so protected from availing of the opportunities offered in the Teachers' Insurance and Annuity Association constitutes a remarkable situation and involves a grave responsibility toward younger teachers in a matter very closely affecting the interest of younger men—a responsibility to be undertaken only after most thorough consideration.

The policies offered in the Teachers' Insurance and Annuity Association are so favorable that in time they will make their way. At the present date (July, 1919) the new company has written $700,000 of insurance and annuity contracts for $87,000 annually. A score of institutions in the United States and Canada, including several thousand teachers, have asked to co-operate with their teachers in the purchase of old age annuities through the Teachers' Insurance and Annuity Association. The trustees of this Company have nothing to do with the relations of the Carnegie Foundation to its associated institutions. Their duty is simply to conduct the Teachers' Insurance and Annuity Association, as the law directs, in the interests of the policy-holders. In carrying out this endeavor they welcome any co-operation with your Committee or with any other group of college and university teachers. The trustees do not, however, consider that your Committee is in a position to offer expert advice touching technical questions of the organization and operation of an insurance company such as those to which your

letter refers. In these matters they have endeavored to obtain the best expert advice to be had in America and Europe.

I understand that it is your intention to publish your letter as well as this reply in the BULLETIN of the Association.

I am very truly yours,

HENRY S. PRITCHETT.

6. *President Pritchett to President Lovejoy*

SANTA BARBARA, CALIFORNIA, August 23, 1919.

Dear Mr. Lovejoy:

Your letter of August 3rd has just been forwarded to me from New York. In the meantime, my reply to your letter, which was nearly a month old, had been sent to my office to be copied and forwarded. It only got back to me yesterday, and I signed it and sent it on to you.

You will understand that I desired to obtain from various trustees of the Teachers' Insurance and Annuity Association any opinions they might care to express, and it was impossible to carry out this correspondence any more rapidly than it was done.

Yours very truly,

HENRY S. PRITCHETT.

7. *President Lovejoy to President Pritchett*

OAKLAND, CALIF., August 29, 1919.

My dear Mr. Pritchett:

Your letter of July 27th, in reply to mine of June 27th, came to hand a few days since, and was shortly followed by your note in which you were good enough to explain the causes of the delay in your reply.

I am not able to judge from what you say whether the suggestions contained in my former letter have or have not been formally submitted to, and acted upon by, the Board of Directors of the Teachers Insurance and Annuity Association. If not, I would request that my letter of June 27th be regarded as a communication to the Board and be laid before that body at its next meeting. Meanwhile I take occasion to comment upon certain points in your reply. The only portion of it which appears germane to the practical questions which I raised—the questions of participating policies and mutualization—consists of the third to the seventh paragraphs. It is to those that I shall first, and chiefly, address myself.

I. Your letter seems to show that the remarkable nature of the proposal at present made to college and university teachers by the Teachers' Insurance and Annuity Association is not yet evident to you. What is proposed is this: that these teachers shall place in the hands of the new company—not of its present Board of Directors merely, but of future Boards not known to the teachers and not to be chosen by them—sums which should in time exceed by hundreds of thousands of dollars the actual cost of the insurance furnished, without the Company's assuming any legal obligation, or even definitely expressing any intention, to return this excess to the policy-holders. That is the plain, outstanding fact of the situation. I submit that the surplus in question ought to be regarded —as in all mutual companies it is regarded—as the property of the policy-holders;

that, consequently, legal title to it ought in some form to vest in the policy-holders; and that an arrangement by which they have no legal claim to the divisible surplus resulting from their payments, no legal or other remedy if it should ever be used in ways which they regard as not to their interest, and no control of the company, is a grossly unbusinesslike arrangement, and is in obvious conflict with the sensible warning previously issued to teachers, by yourself and others, against "accepting any arrangement less secure than a contractual one" when the safe-guarding of the future of the teacher, or his dependents, is at stake. A man of good sense and good feeling is usually unwilling to receive any considerable fiduciary funds, even from his most intimate friend, without signing some document which will legally bind both himself and his estate to the return of those funds. Yet in this case it is proposed that teachers shall deposit a fund (*i. e.*, the accumulated surplus) which should be regarded as fiduciary, in the hands of a corporation which may in a short time be composed of persons wholly unknown to the depositors, receiving from that corporation not even a verbal declaration of intention with respect to the return of the fund—receiving, rather, a formal declaration that the depositors have no claim to its return.

There is nothing in the present charter and contracts of the company which could prevent any future Board of Directors from accumulating the surplus for a long period of time without distribution; or from devoting the surplus to "the benefit of teachers" in ways in which teachers do not wish to be benefited; or from erecting an expensive building for the company out of it; or from using it to increase the salaries of officials; or from employing it in stock manipulation. Such things as these have happened in the history of American insurance companies; and, before the enactment of the remedial legislation of 1906, they happened even in some of the great mutual companies, whose directors, men of high standing in the community, were supposed to be bound to act only in the interest of the policy-holders. The reasons which made that legislation necessary for the protection of policy-holders, with respect to their interest in the companies' surplus, are reasons which will make a prudent man hesitate to purchase his insurance in a company in which he will lack that legal protection.

In saying these things I of course imply no reflection whatever upon the present Board of Directors of the Teachers Insurance Association. I obviously could not do so, since most of the gentlemen who compose the Board are personally unknown to me, and, I suppose, to the majority of college and university teachers. I have no doubt of the earnest desire of the present Board to be of service to teachers and to the cause of learning and of education. It is because I assume this that I find it difficult to suppose that, when the Board as a body gives serious attention to the considerations above mentioned, and to those presently to be added, it will fail to recognize the unsoundness of certain features of the company's present policies and organization, and their incongruity both with the purposes for which the Company was founded and with the rules of ordinary business prudence and of practical good sense. For it plainly is not customary with business men, or other sensible men, to place moneys which—or the interest on which—they desire or expect to have returned to them, in the hands of any institution or corporation which expressly and formally refuses either to contract or to promise to refund those moneys. If, for example, I wish to receive interest on my savings, I do not by preference deposit them in a bank, however philan-

thropic its purposes, which announces itself as conducted exclusively on a "non-interest-paying basis." As has been well pointed out in the recent pamphlet of your company, "in dealing with the Teachers' Insurance Association, teachers are concerned only with questions that pertain to all insurance companies." It is, I take it, inconceivable that the officers, or the Committee on Pensions and Insurance, of this Association should advise members who desired to receive the benefit of the surplus accumulated out of their payments, to take insurance in any *other* company which should make a proposal similar to that of the Teachers Insurance and Annuity Association.

The Teachers Insurance Association either does or does not intend to regard its eventual divisible surplus as the property of its policy-holders, and to distribute that surplus to them in the manner which they may elect. If it does so intend, there is every reason why it should say so. Why, then, does it not say so?

II. To this question we receive the reply that it was "practically impossible" to organize the new company as a participating company. We have repeatedly asked wherein the practical impossibility consisted, and have received a series of curiously diverse replies. We have often been asked, as in certain passages of your letter, to accept the necessity on the authority of "the best," but modestly anonymous, "legal and expert advice." Acceptance of conclusions of importance upon the authority of anonymous persons is a practice not common among university teachers; nor are such teachers as a rule incapable of understanding the reasons for a conclusion, if carefully explained to them. There is, I suppose, no other body of men, unless it be the members of the legal profession, with whom the tone of kindly condescension to ignorance and unsophistication—a tone, may I say, not without exemplification in your letter—is less likely to be effective. It must be added that our profession has had opportunity to judge by experience of the value of the expert advice enjoyed by the Carnegie Foundation. When the Foundation was established in 1906 it was announced that "expert calculation" showed that the original endowment would be ample to carry out the program of pensions then promulgated. The subsequent history of the Foundation is sufficient commentary upon that "expert calculation."

We have, however, been offered certain "reasons," as well as the unquoted opinions of unnamed authorities, in support of the contention that the organization of the new company, under a New York charter, on a participating basis was "practically" impossible. The earliest of these reasons, and for a time the only one given, was that "distributions on a participating policy issued at net rates would be so small during the first years of its existence that if distributed in annual dividends they would not in some cases pay the cost of postage" (12th Annual Report, p. 46). This appears to have been seriously put forward with the expectation that teachers would be persuaded by it that they should be content with non-participating policies and that mutual insurance companies are undesirable things. Comment upon this "reason" seems superfluous.

In your letter, however, and in the recent publications of your company, an explanation for the non-participating character of the new company's policies is found in Section 97 of the New York Insurance Law. By this section companies organized on the participating plan must pay all expenses of operation out of premiums, and must consequently load premiums sufficiently to cover such expenses. If the Teachers Insurance Association were incorporated on a partici-

pating basis, it would be compelled to increase its premiums by the amount of this loading, and would be unable to pay its running expenses, as it now does, out of the interest on its endowment. This, it is argued, would be to the detriment of the policy-holder, since it would mean that he would pay considerably more for his insurance.

This argument, however, as I pointed out, in effect, in my previous letter, tells only half the story. It is as if one were to estimate the value of a man's estate by enumerating his debts and disregarding his assets. For if the Teachers Insurance Association were a mutual company the policy-holder could, and would, share in the earnings of the company's original capital of one million dollars; and the dividends thus received by him would, in all probability, much more than offset the increased loading of his premiums required by Section 97 of the New York law.

To this you reply that such an arrangement would be "an evasion of the law." You will permit me to say that this reply is more concise than convincing. It embodies what I can only describe as a rather astounding conception of the import of the law of insurance; for it implies that any arrangement permitting policy-holders to share in the earnings of a company's invested funds—*e. g.*, its organization as a mutual company—would be an "evasion of the law." Obviously, any mutual company would be one in which the plan suggested in my previous letter would be lawful and normal. And it is manifestly absurd to say that the existence of a mutual company is, as such, an evasion of the law. What, once more, the law says is that for each calendar year expenses of operation in a participating company shall not exceed the loading on premiums *plus* the present value of certain assumed mortality gains. For that the plan suggested in my previous letter expressly provides. The law does not say, and it assuredly does not intend, that policy-holders in a mutual or other participating company shall not, after this condition is met, be permitted to benefit by the surplus earnings of the company, from whatever part of the company's assets derived. Upon this point I quote once more the statement of the New York Superintendent of Insurance, an authority whom you appear to respect:

"I do not know of any provision of the law which would prohibit a company operating on a participating plan from distributing the earnings from *its capital stock* and surplus to its policy-holders in the form of dividends."

If, however, you still remain in doubt upon the point, I would suggest that measures be taken to get it definitely settled; and I therefore invite you to submit to Charles Evans Hughes, Esq., George Richards, Esq., or any member of the New York Bar recognized as especially conversant with the insurance law of that state, the following specific questions:

"(1) If an insurance company, organized under the laws of New York, with a charter authorizing it to write participating policies, receives a certain sum, say, $1,000,000 as a free gift for the benefit of its policy-holders, is there anything in the law forbidding it to pay the interest, or any part of the interest, accruing on this sum to the policy-holders in the form of dividends or of reductions in premiums?

"(2) If the answer to the preceding question is in the negative, is there anything in the law which would forbid such a company to *announce* that it will pay to policy-holders all, or some specified part, of whatever interest may be earned

by the sum thus acquired by gift—it being understood that the operating expenses and legal reserve have been provided for by the loading on premiums?

"(3) Specifically in the case of a *mutual* company, part of whose assets have come to it by donation, is there anything in the law forbidding the Company to distribute the earnings from its invested funds (including such donations) to its policy-holders in the form of dividends—assuming, as in question 2, that all requirements of the law with respect to reserve, etc., have been met?"

You raise one further difficulty with respect to participating policies: namely, that "there would still remain the problem of conducting the company within the amount furnished by loadings on policies which during the first years of the existence of a company would be wholly inadequate to bear the expense of the most conservative business." Here again, however, appears to be a piece of reasoning analogous to estimating an estate on the basis of debts to the disregard of assets. Let it be supposed that the Company's expenses for its first year are $25,000 and that it has only the 500 subscribers required by Section 71 of the New York law for the beginning of a mutual company. Each subscriber would, in that event, pay a loading on his premium of $50 for expenses of operation—less the amount deducted under the provision relating to assumed mortality gains. But he would have the prospect of sharing at the end of the year, not only in any surplus earnings on his own payments, but also in the interest on $1,000,000—say fifty thousand dollars—none of that sum being any longer required for expenses. The policy-holder, in short, could not be the loser and would probably be the clear gainer by the arrangement, and would, consequently, be very ready to pay the additional loading necessary to make such an arrangement possible under the law. In proportion as the number of policy-holders increased, the loading could be diminished, and concurrently the *per capita* participation in the earnings of the endowment would decrease.

Thus none of the reasons offered for the determination not to offer participating policies will bear analysis. But you again refer me to authority—in this case that of the Superintendent of Insurance of the State of New York. You remind me of a letter of that official to me, of date of May 31, in which you say he "makes clear the fact that the organization of a new company on the mutual plan is practically impossible." I note, I confess, with some surprise that you have thought best to refer to the communications of Superintendent Phillips, which are marked by some rather singular features of which you are not unaware. Let me recall the circumstances. In reply to certain specific inquiries of Dean Stone and myself, Mr. Phillips wrote us on April 21, 1919, a letter which he does not permit me to reproduce—but which every officer of the Association who has seen it regards as fully substantiating the view that there were in the New York law no insuperable "practical" obstacles to the establishment of the new company on a participating basis. When asked to permit publication of this letter, Mr. Phillips declined to do so until after he had communicated with you. A month later his letter to which you refer was received—a letter very different in its tenor from the one which he had written before he had had the benefit of consulting with you. The conclusion which it was manifestly intended to convey was such as you have indicated; it was, in fact, a labored *apologia* for what had been done by your company, with explanations of the views and purposes of the incorporators and other apologetic material irrelevant to the specific questions

asked. Nevertheless, we should have attached some weight to this document if its author, in addition to stating (in somewhat ambiguous terms) a conclusion, had not also stated his reasons for that conclusion. The reasons, however, were all completely and conspicuously lacking in pertinency to the particular case of a company like the Teachers Insurance Association; and no great acumen was required to perceive that, in fact, they proved exactly the opposite of the conclusion intended. Mr. Phillips, for example, urged at length that "a mutual company or a stock company on the mutual plan which is in the process of organization would have no resources from which it could pay the initial expenses of organization, such as legal fees, printing of policy forms, etc., etc., *except such funds as might be donated*, or, if a mutual corporation, loaned to it in accordance with the provisions of Section 71, New York Insurance Law. *The conditions under which such funds can be obtained in either of the above ways are not often found in the business world*" (italics mine). Mr. Phillips' reasoning would apparently run thus: 'A company cannot be established on a mutual or participating plan unless funds out of which expenses of organization can be paid are either donated to it or borrowed by it; the Teachers Insurance Association *had* such funds donated to it; therefore, it could *not* be established on a mutual or participating plan.'

The same statement observes: "With the large number of life insurance companies transacting business at the present time and furnishing full opportunity for the public to secure insurance protection, there is no such incentive [as formerly] for starting mutual companies." This, surely, is a little masterpiece of irrelevancy. No one who reads this "official statement" (it will be published in full in the next BULLETIN) will be likely to share your surprise that the officers of this Association were not convinced by it of the practical "impossibility" of the organization of the Teachers Insurance Association as a participating company. What we were convinced of by the statement was that the usual difficulties in the establishment of a new mutual company do not arise in the case of a company possessing a free initial capital of one million dollars.

We have, however, always found the statements of the New York Department of Insurance accurate and trustworthy when they consist, not in involved essays in apologetics in behalf of the present policy of the Teachers Insurance Association, but in direct replies to definite questions concerning the actual provisions of the insurance laws of the state. And the whole issue, with regard to the practicability of converting the Teachers Insurance Association into a participating company under the present statutes depends upon the single, and the exceedingly simple, point of law already mentioned—viz., the question whether there is anything in the law to prevent a participating or mutual company from granting its policy-holders a share in the earnings of its invested funds, thereby—in the case of a company having capital received by donation—offsetting the additional loading of premiums required of participating companies. Upon this question the reply of the State Superintendent of Insurance has already been quoted above; and it unequivocally sustains our contention.

I may add that if, for any reason, the Teachers Insurance Association is still averse from the simple and obvious method pointed out in my previous letter for its conversion into a participating company, there is more than one other way by which the same desirable change can be accomplished—if the directors of the company really wish to accomplish it. For example, it can scarcely be doubted

that the New York legislature would readily pass an amendment to the present insurance laws, providing that companies receiving, by gift, an endowment to be used for the benefit of the policy-holders may, subject to regulations prescribed by the Superintendent of Insurance, pay necessary expenses of operation out of the income from this endowment. If the directors of your company should desire to adopt this way of dealing with the situation—though, in reality, no new legislation is necessary—I am sure that the members of the Association of University Professors resident in New York would gladly use their influence as citizens of that State in behalf of the measure suggested.

Since, then, there is no insuperable, or even serious, obstacle to the conversion of the Teachers Insurance Association into a participating company, a continued refusal of such conversion on the part of the company will necessarily be construed by college and university teachers as evidence that those who determine the company's policy are, not unable, but unwilling, to afford policy-holders any legal assurance of participation in the surplus—the potentially large surplus—which will be accumulated out of the payments of teachers and institutions. Is it the desire of the directors of the company to force that inference upon those for whose benefit the company was established and upon whose confidence, interest and sympathy its success must depend?

III. The greater part of your letter refers to various matters of past history to which there is, I think, little profit in adverting. It contains, however, certain misstatements of fact which should not go wholly uncorrected. You state, for example, that this Association "circulated among its members the statement put forth by the Provident Life and Trust Company in the endeavor to sell its own policies"; and again that "an advertising effort of a commercial insurance company" was "circulated through the agency of the American Association of University Professors and ostensibly with its approval." These statements are not in accord with fact; and that they are not, you have already been informed, in reply to your own inquiry upon that point, of February 21, 1919. The pamphlet to which you refer was circulated by the Provident Life and Trust Company and at the expense of that company. The author of the pamphlet, at the suggestion of a personal friend who is a member (not an officer) of the Association, requested, through this friend, permission to obtain from the printer of the BULLETIN the Association mailing list and to employ the same printer to do the addressing. This courtesy was readily granted Mr. Linton; it would as readily be granted yourself or any other person desiring to communicate with members of the Association. These facts were made known to you by Dean Stone in his letter of February 24, and were again stated in his letter of April 3. May I, therefore, request that you will cease to give currency to a wholly misleading version of this incident?

I must add that I am not able to take so gloomy a view as yourself of Mr. Linton's pamphlet. Whatever its motive (of which I have no occasion to judge) it contained information and arguments with regard to the relative value of certain types of policy (irrespective of the company issuing them) which it was desirable that our members should consider. Nor does it appear to me that the pamphlet which your company has thought it appropriate to name "Some Misapprehensions Touching Life Insurance" is an altogether conclusive discussion of the matters upon which it touches. It may interest you to know that we propose to pub-

lish in the next BULLETIN an article by Mr. Linton—who is, as you know, a distinguished actuary, though not one of those in the service of the corporations of which you are the head. This article, you will find, is in no sense "an advertising effort of a commercial insurance company," but an expert's discussion of certain points of insurance theory. It contains, however, a careful examination of the reasonings upon the same points contained in your company's pamphlets.

IV. You inquire "what other things the Trustees of the Foundation could have done," beyond what they have actually done, "to show a desire for friendly co-operation with the Association of University Professors." If the practical matter before us concerned the Carnegie Foundation, and not the insurance company, your question would assuredly be entitled to an answer; and the answer would be a long one. But as the question is scarcely relevant to the business in hand, I will only mention, as it were by title, four things which might with advantage have been done by the trustees of the Foundation, if they desired to make it possible for this Association to co-operate actively and cordially in the carrying out of the Foundation's policies:

(a) The trustees of the Foundation, before suddenly adopting the present plan for the insurance company, with its wholly unanticipated and unforeshadowed features, might have submitted that plan for consideration and report to the Joint Commission appointed in 1917; or, preferably,

(b) They might have adhered to the plan recommended unanimously by the Joint Commission (including the Foundation's representatives thereon), together with the supplementary provision suggested in the Report of our Committee in 1918, that "in the organization of the insurance company suitable provision be made whereby, within a reasonable time, if not immediately, the power to elect the Company's trustees or directors shall be vested in the policy-holders, in proportion to their contribution to the financial resources of the company."

(c) The Foundation might have demonstrated its "scrupulous regard for the privileges and expectations created under existing rules" by refraining from making retroactive, by more than two years, the action taken in April, 1918, repealing its existing rules.

(d) The trustees of the Foundation might have adhered for at least one month to the assurance given in their Minute of November 21, 1918, in response to certain resolutions of the Committee on Pensions and Insurance of this Association. Yet the Foundation's Circular of December 6, 1918, was in conflict with that Minute, inasmuch as it announced the trustees' intention to devote a part of the income of the Foundation to some other purpose than the discharge, as nearly as possible, of the obligations in force on November 5, 1917.

V. I confess that I miss the point—though not the purpose—of your paragraphs referring to the fact that "most of the members" of our Committee on Insurance have claims to retiring allowances in the Carnegie Foundation, while our "younger colleagues" have no such claims. I had supposed that the Teachers Insurance Association was offering to sell life insurance to all college and university teachers, whether they are potential pensioners or not; that the question whether the offer should be accepted is one that concerns both the private interest of every teacher and also the interests of the profession and of institutions; and that, if the present policies and method of organization of the Teachers Insurance Association are unsatisfactory from the point of view of possible policy-holders, that fact is, if

anything, of even more concern to the younger men in the profession than the older. The criticisms upon your company's present policies and organization which we have been compelled to make are general criticisms applicable to non-participating policies and non-mutual organization as such; and either they are valid or they are not valid. Their validity does not depend upon the age of the person who makes or who reads them but upon the reasons by which they are supported.

It is, perhaps, worth while to add that this Association has already had the privilege of assisting in rendering a material service especially to the younger men of the profession. The Carnegie Foundation's circular of December 6, 1918, proposed to the American colleges and universities a plan of compulsory and contributory annuities. This plan would have compelled a young teacher who is supporting a wife and children on his salary to set aside approximately 10 per cent of his professional reward in order to obtain an annuity for himself thirty or forty years later, and would thereby, as a rule, have deprived him of the means of obtaining what he needs very much more—viz., adequate insurance for his dependents during the period before his children become self-supporting. Against this extraordinarily ill-considered scheme the Association protested promptly and emphatically, both through published pamphlets and through the efforts of its local branches in many institutions. The compulsory feature of the plan, so far as the Foundation is concerned, was, as you know, abandoned by the action of the trustees on February 26.

VI. I note with interest the figures concerning the new insurance company's business of which you inform me. The directors will, I have no doubt, see in those figures evidence confirmatory of what I said in my previous letter concerning the prevailing attitude of university teachers towards the present non-participating policies of the Company. For the facts you mention would seem to show that, in view of the Company's very extensive advertising, surprisingly few policies have been sold. You do not indicate the average value of the policies issued; but even if it be as little as $4,000 the figures given would mean that only 175 teachers had bought life insurance policies. The total is less than the minimum required by the New York law—one million dollars, with five hundred subscribers to policies—before a *mutual* company can be legally regarded as a going concern. The same indication of the feeling of the teaching profession may be seen in the fact that only twenty institutions had, at the end of the academic year, accepted the Carnegie Foundation's proposals for the establishment of contributory annuity systems—especially when it is borne in mind that some of the twenty took this action without the knowledge or approval of their faculties. Even if the figures you give were doubled, one would still be compelled to conclude that the Company's policies are very far from generally acceptable to those for whom they are intended. The experience of the Company thus far, then, as well as more weighty considerations, may well give the directors grounds for reconsidering those features of the present plan of organization and type of policy to which the representatives of this Association have more than once called attention. I am,

Very truly yours,

Arthur O. Lovejoy.

8. President Pritchett to President Lovejoy

SANTA BARBARA, CALIFORNIA,
September 25, 1919.

PROF. A. O. LOVEJOY,
Johns Hopkins University,
Baltimore, Maryland.

My dear Sir:

I beg to acknowledge your letter of date August 29. The various questions raised in your communication have been completely answered in my former letter, and in the small pamphlet to which I have already called your attention. Your last letter impresses me as an effort in the direction of attaining "rather commendation of wit in being able to hold argument than of judgment in discerning what is true." There seems no occasion for a further communication on my part.

The Teachers' Insurance and Annuity Association has now had six months of business. It has written insurance contracts of three-quarters of a million dollars, and annuity contracts which represent a total business of a million dollars more. The company is so organized as to give to its policy-holders a service which no commercial agency can approach, and to offer to its policy-holders in due time, a real representation in the management of the company, instead of a fictitious representation. It may be necessary to await the actual experience of a few years in order to demonstrate to teachers the great advantages offered to them through the policies of the association. This experience will no doubt be the best answer to the misapprehensions and doubts which have been raised.

It may have escaped your attention that the relations of the Insurance and Annuity Association to Canadian teachers in higher institutions of learning are exactly the same as to teachers in colleges and universities of the United States. I note that, while the association of which you are president bears the name "American," it has not as yet admitted the professors of Canadian universities. In Canada there is no demand on the part of university professors for the mutualization of the Teachers' Insurance and Annuity Association, for the reason that in Canada the insurance companies chartered under Canadian laws are, practically without exception, stock companies.

Yours very truly,
HENRY S. PRITCHETT.

9. President Lovejoy to President Pritchett

October 3, 1919.

My dear Mr. Pritchett:

I beg to acknowledge receipt of your letter of September 25, replying to mine of August 29. In view of your attitude towards all suggestions for the modification of the present form of policy and organization of the Teachers Insurance Association, there would seem, as you intimate, to be little advantage in continuing the correspondence. I feel obliged, however, to remind you of my request—to which your reply makes no reference—that my letter of June 27, which included a suggestion of a conference between the Board and representatives of this Asso-

ciation, be regarded as a communication to the Board of Trustees of the Insurance Association, and be laid before that body at its next meeting for such action as it may think fit to take.

I also beg to remind you that my previous letter contained a proposal—which likewise seems to have been overlooked in your reply—that the principal point at issue be submitted for decision by some competent legal authority not connected with either association. Your stated reason for objecting to participating policies has now resolved itself into a single proposition—viz.: that there is something in the New York insurance law which would forbid policy-holders (if the company were a mutual or other participating one) to share in the earnings of the company's invested capital or endowment in such a way as to offset the expense-loading on premiums which is required of participating companies. You will, I trust, be willing to concede that this opinion on a point of law may conceivably be erroneous, inasmuch as it does not appear to be put forward by any member of the legal profession, and is in conflict with the opinions on the subject which have been expressed by the Dean of the Columbia Law School and the State Superintendent of Insurance of New York. The question whether the company shall or shall not offer participating policies is perhaps as important, from the point of view of teachers and from that of the company, as any which can come before the trustees for consideration; and the reason which determines their decision upon this question ought not to be open even to any serious doubt. I therefore formally request that the Board of Trustees state officially whether it holds or assumes that there exist provisions of the New York law which would prevent policy-holders in the company, if it were organized on a participating plan, from sharing in the earnings of its capital, after all requirements of the law as to reserve, loading, and the like, had been met. Or, if the Board is not prepared to state its position on this fundamental question at the present time, I request, as an alternative, that the Board obtain the opinion on this question—which is formulated more fully on page 8 of my previous letter—of Mr. Hughes, Mr. George Richards, or any other New York attorney recognized as an authority on insurance law, with the understanding, of course, that the opinion received will be published. Finally, I shall be obliged if you will lay this letter, along with that of June 27, before the Board of Trustees of the Insurance Association.

Very truly yours,

A. O. Lovejoy.

II. Correspondence with the State Superintendent of Insurance of New York

The following correspondence has taken place between officers of the Association and the Superintendent of Insurance of the State of New York.

1. President Lovejoy to Superintendent Phillips.

March 28, 1919.

Dear Sir;

This Association is greatly interested in the plans of the new Teachers Insurance and Annuity Association recently incorporated under the laws of the State of New York, for the especial purpose of providing insurance and annuities to college and university teachers upon advantageous terms. This company is as you, of course, know an offshoot of the Carnegie Foundation, and has been started with an endowment of one million dollars, given it by the Carnegie Corporation. It was, presumably, the idea of the trustees of the Carnegie Corporation that the interest upon this endowment should be used to pay the running expenses of the Insurance Company, so that the entire accumulation from premiums paid by teachers might accrue to the benefit of the teachers holding policies in the company. The new company, however, offers only non-participating policies and is forbidden to write participating policies by the terms of its charter.

Our Committee on Pensions and Insurance, of which Dean Stone of the Columbia Law School is chairman, has recently submitted and published a report upon the plans of the new insurance company, and has taken serious exception to the non-participating character of the policies offered. The Committee points out that teachers taking insurance in the company are contractually guaranteed 4 per cent interest on accumulated premiums but will have no legal basis whatever for claiming a share in any surplus income beyond 4 per cent which the company may be able to obtain—and which it seems not unlikely to obtain, in view of the selected character of the risks, the extremely low cost of doing business, and the possession of a free initial capital of one million dollars.

To these objections to the non-participating feature of the new company, its president, Dr. H. S. Pritchett, has stated, in speaking to several college faculties, that it was impossible to establish the Teachers Insurance and Annuity Association as a participating company, because of a provision of the New York insurance law requiring, in the case of a participating company that running expenses, as well as the reserve, be set aside out of premiums before any dividends are paid. Mr. Pritchett has argued that, especially in the first years of the new company, this requirement would be prohibitive of the writing of participating policies; the running expenses could not be paid out of the endowment if the company offered such policies, but the amount of the premiums would not at first be sufficient to cover those expenses, still less to make possible the payment of any dividends.

Dean Stone, however, has expressed the view that there would be no serious obstacle to the writing of participating policies by the new company; that all that would be necessary would be for the Teachers Insurance and Annuity Association to place upon the premiums sufficient loading to cover the expenses, while at the same time adding to the surplus the income from its endowment. The difference between this arrangement and the payment of running expenses directly from the

endowment would apparently not be more than a matter of bookkeeping; and the practical result to the policy-holder would in the end be virtually the same as if the expenses had been paid from the endowment and dividends had been paid from premiums. If any special difficulty were encountered during the first two or three years in the history of the new company, it has been suggested that the company, if made a participating one, could insert in its contracts a provision that policy-holders shall be entitled to participate in dividends only after premiums have been paid for two or three years. In view of the importance of this matter to a large number of college and university teachers in New York and in other states, I shall be greatly obliged if you will inform me upon the following points:

1. Was there, in your opinion, any insuperable obstacle to the establishment of the Teachers Insurance and Annuity Association as a company offering participating insurance to those desiring it?

2. Is there, in general, any serious legal difficulty in the establishment of a participating insurance company under the laws of the State of New York, provided the premiums be loaded sufficiently to provide for the legal reserve and the expenses of conducting the company?

3. Is there any legal or other obstacle to the offering of insurance or annuity contracts containing the provision that the policy-holder shall not be entitled to dividends until after premiums have been paid for two or for three years?

I shall, of course, be grateful for any further information upon matters above referred to, not covered by the preceding questions, which you may be kind enough to furnish me. You have, I think, already received a copy of the report of the Committee of which Dean Stone is chairman.

I enclose stamped and addressed envelope.

Very truly yours,

A. O. LOVEJOY.

Superintendent Phillips replied to this inquiry on April 21; the general nature of his reply is indicated in President Lovejoy's letter (No. 8 in the preceding correspondence). To a request for permission to communicate this reply to the members of the Association through the BULLETIN, Mr. Phillips replied as follows:

2. Superintendent Phillips to President Lovejoy.

ALBANY, April 28, 1919.

Dear Sir;

We have for acknowledgment your letter of April 24, regarding the Teachers Insurance and Annuity Association. You request permission to publish our letter of April 21 in a BULLETIN to appear late in May.

It appears that some of the points discussed in our letter are in controversy between your Association and the Teachers Insurance and Annuity Association. As our letter was not prepared for the purpose of publication we shall request you not to print it until we have given Dr. Pritchett an opportunity to present his objections, if any.

We will advise you further as soon as possible.

Yours very truly,

JESSE S. PHILLIPS.

Nothing further being received during the following month, a second request for a reply to the questions previously submitted was sent to the New York Department of Insurance on May 26. The following answer was received:

3. Superintendent Phillips to President Lovejoy

May 31, 1919.

Dear Sir;

Re; Teachers Insurance and Annuity Association of America.

Referring to the correspondence which this Department has had with yourself and Dean Stone of the School of Law, Columbia University, in reference to the above Association, I desire to make the following statements:

The letters ordinarily sent out from this Department in answer to inquiries and complaints are not written with the view that they will be published.

In carrying on the immense volume of correspondence of this Department, it is impossible to go into all of the various phases of every matter touched upon in such correspondence and the possible interpretations of the meaning which may be placed upon our statements in reference thereto.

It is therefore quite possible that in some cases injury and injustice may be done to both this Department and the outside persons or interests involved, if the correspondence is used for other purposes than that for which it was intended.

I would, therefore, suggest that, if you or your Association should hereafter desire statements from this Department which you may wish to use in a public manner, this fact should be stated in your inquiry. In other words the request for publicity should more properly be made at the inception of the correspondence rather than later.

The correspondence shows an apparent inconsistency in so far as Dr. Pritchett has made the statement that it was impossible to organize a participating company under the limitations and restrictions of the New York Insurance Law, whereas this Department has made statements which might perhaps be construed to the contrary. The Department has also made a statement to Dr. Pritchett which would apparently justify his contention that it was impossible to organize a new participating company under the New York Insurance Law.

However, I believe an examination of the whole matter will show that there is no inconsistency in the statements of either Dr. Pritchett or this Department. Dr. Pritchett doubtless referred to the opinions of men well qualified in life insurance matters who were consulted by him and who held the view that it was practically impossible to organize a successful new participating company under the laws of this State.

The Department's letter in which it was stated that it is not impossible to organize a mutual company or a stock company transacting participating business under the New York Insurance Law refers to the matter from the legal point of view. In other words, the Law does not either expressly or by implication prohibit the organization of a mutual company or the organization of a stock company on the mutual plan.

However, it appears that a strict compliance with the provisions of Section 97,

New York Insurance Law, makes the organization and operation of a mutual life insurance company or of a stock company on the mutual plan practically impossible, under ordinary conditions.

A mutual company or a stock company on the mutual plan which is in the process of organization would have no resources from which it could pay the initial expenses of organization, such as legal fees, printing of policy forms, supplies, office rent, salaries of employees, etc., except such funds as might be donated or, if a mutual corporation, loaned to it in accordance with the provisions of Section 71, New York Insurance Law.

The conditions under which funds can be obtained in either of the above ways are not often found in the business world.

A mutual company or a stock company on the mutual plan, which has already commenced business, cannot contract for or pay expenses except out of assumed mortality gains and loadings contained in premiums on its outstanding policies. See Section 97, New York Insurance Law.

In view of the above facts, the persons interested in the organization of the Teachers' Insurance and Annuity Association came to the conclusion that it was not practicable to organize it on a mutual plan.

In the opinion of this Department, the organization of a mutual company under the laws of any state in the Union is not practicable under ordinary conditions inasmuch as, in order to pay the initial expenses and put up the required reserves, there must be a surplus fund contributed in some way to the company and this can only be done through capital stock subscriptions or a guarantee fund or some similar method.

A large number of the most successful mutual life insurance companies in the country today had to have so-called "guarantee funds" contributed in the early days of their history by interested persons, who hoped to have such funds returned to them with interest, if the companies were successful. With the large number of life insurance companies transacting business at the present time and furnishing full opportunity for the public to secure insurance protection, there is no such incentive at the present time for starting mutual companies.

At the inception of the Teachers Insurance and Annuity Association, there were long discussions as to how the Association should be organized. It was the express desire of the organizers that all of the profits should go to the policy-holders and that it should be so provided in their charter. However, this Department advised them that if they organized as a non-participating company, they could not provide either in their charter or in their policies for any distribution of surplus. This advice was given in accordance with the provisions of Section 83, New York Insurance Law.

The following two points were involved in the question of whether the Association should be a participating or a non-participating company:

First: As a going participating company it would have no legal right to contract for or pay expenses except out of assumed mortality gains and loadings contained in premiums on its outstanding policies. This point has already been discussed in this letter.

Second: As a participating company it would be required to distribute its profits annually. The organizers of the Association objected to an annual distribution of surplus.

One objection which the organizers had to such a distribution of surplus was that, inasmuch as the company did not expect to build up a regular agency organization, it would have to depend, to a certain extent, upon the putting out of policies at lower premium rates than the regular old line companies in order to successfully compete with them for business. Low premium rates necessitate small loadings on the net premiums. The net premiums are the same for all companies using the same mortality and interest assumptions. The only way that premium rates can be increased or decreased, the mortality and interest assumptions remaining the same, is by an increase or decrease in the loading.

It would accordingly follow that, if the Association adopted lower premium rates than the old line companies, it might not have a sufficient amount of assumed mortality gains and premium loadings to pay its running expenses. Under the provisions of Section 97, New York Insurance Law, it would not be permitted to use any part of the large income from its invested assets for expenses, even though the excess interest earnings over the required amount might be considerable.

Furthermore, with such low premium rates, the dividend results might prove disappointing to the policy-holders. As a matter of fact, it is quite possible that the Association may not be able to earn any profits.

The organizers of the Association appear to have been willing to attempt its organization on a participating basis, if they could have provided for the distribution of surplus at the end of five year periods instead of annually. They were advised that such a distribution was prohibited by Section 83, New York Insurance Law.

The object of the Association is to provide insurance for college professors and teachers at net cost. It does not contemplate the accumulation of profits. But if there should later prove to be an accumulation of profits, I would call your attention to the clause in the Association's charter which specifically prohibits the distribution of such profits to the stockholders.

A non-participating company undoubtedly has the legal right to make a voluntary distribution of profits to its policy-holders. However, it should be noted that such a distribution of profits is entirely voluntary. The Association cannot promise such a distribution of profits either in its literature or its policy contracts, nor can it represent in any manner whatsoever that it is conducting a participating business.

The following is a summary of the conclusions which represent the views of this Department:

1. It is not legally impossible to organize a mutual life insurance company or a stock company on the mutual plan under the New York Insurance Law.

2. It is practically impossible under ordinary conditions to organize a mutual life insurance company or a stock company on the mutual plan under the New York Insurance Law, with particular reference to the restrictions contained in Section 97.

3. It is practically impossible for a new life insurance company charging low premium rates to do an avowed participating business under Sections 83 and 97, New York Insurance Law.

4. If the charter or policy contracts of a life insurance company provide for any distribution of surplus, or if the company in any way represents itself as con-

ducting a participating business, it must make an annual distribution of its earnings in accordance with the provisions of Section 83, New York Insurance Law.

5. Notwithstanding the above facts, experience has shown that the restrictions and limitations of the New York Insurance Law were necessary in order to control the large insurance corporations in this state and require economy in their operation.

I have no objection to your publication of this letter provided it is published as a whole.

Respectfully yours,

JESSE S. PHILLIPS.

4. Chairman Stone to Superintendent Phillips

June 3, 1919.

Dear Mr. Phillips;

I beg to acknowledge the receipt of your letter of the 2d, in reply to my letter of April 30, and enclosing a copy of your letter of the 31 ultimo to Professor Lovejoy, President of the American Association of University Professors.

I am greatly obliged to you for the information which this correspondence contains. It makes perfectly plain what I had all the while understood to be the case, namely, that there was no legal obstacle to the Teachers Insurance and Annuity Association of America writing participating policies and that there were no practical difficulties in the way of writing such policies other than such as might be involved in having the premiums adequately loaded to meet the expenses of the company and in the annual distribution of dividends, the result being that all policy-holders would have a contractual right to receive their insurance at net cost.

Another point, however, to which both Professor Lovejoy and I have directed our inquiry is whether the Department has taken the position that there was any difficulty either legal or practical in organizing the Teachers Insurance and Annuity Association of America as a mutual company. In your letter to Professor Lovejoy of the 31st ultimo you state that the organization on a mutual plan is practically impossible "under ordinary conditions." This of course we perfectly understood, but the Teachers Insurance and Annuity Association of America was not organized under ordinary conditions. It had resources of one million dollars furnished by the Carnegie Corporation. Assuming that a sufficient amount of its endowment could have been used to meet initial expenses and to create a surplus fund for the insurance company, is there any legal or practical difficulty which would prevent the organization of a company on a mutual basis, and has the Department at any time held that there were any such difficulties?

This letter is an open letter and I shall assume unless otherwise advised by you that your reply may be published.

With much appreciation for your past assistance and thanking you in anticipation for the beneficial information, I am

Yours respectfully,

HARLAN F. STONE

5. President Lovejoy to Superintendent Phillips

June 12, 1919.

Dear Sir:

I have to acknowledge with thanks yours of May 31, written after consultation with the president of the Teachers Insurance and Annuity Association, and containing a second and revised reply to the inquiries in my letter of March 28. While this reply seems, as you have evidently appreciated, at first reading difficult to reconcile with that previously given, in your letter of April 21, I do not find the two, upon analysis, to be in disagreement upon the principal matter concerning which I desired information—at least if I understand your recent letter correctly. I gather from it that there is no difficulty about the establishment of a participating company under the New York law, provided the company is willing to load its annual premiums sufficiently to cover running expenses.

I note, however, your remark that in the case of the Teachers Insurance and Annuity Association, if it had been established as a participating company, the effect of this requirement of the law might have been to compel it to load its premiums to such an extent, during the early years of its operation, that it could not have offered "lower premium rates than the regular old line companies." I do not, however, gather from your letter that there is anything in the law which would prevent the company (if it had been organized on a participating basis) from including in its excess interest earnings, from which dividends might be paid to policy-holders, the earnings on its initial capital of $1,000,000, furnished the company as a free gift for the benefit of its policy-holders by the Carnegie Corporation. If there is any legal provision which would forbid this use of the surplus interest on the company's initial capital, will you kindly indicate the clauses of the New York Insurance Law which would seem to you to have this effect? It is manifest that if the interest on the original endowment of the company were thus used, it would offset the loading on premiums to cover expenses.

In other words, the situation seems to be this: The Teachers Insurance and Annuity Association is an exceptional, if not an unique, insurance company in that it has a free endowment of $1,000,000 given it at the outset to be used for he benefit of such college and university teachers as may purchase policies in the company. It may employ the interest on this sum in either of two ways—either (a) to pay running expenses, or (b) to pay dividends to policy-holders. (a) If it employs the interest on the endowment to pay expenses the company can not offer participating policies under the New York law. But if it does not offer participating policies, policy-holders have no legal claim to share in the excess earnings *either* on the premiums paid by them or on the company's original capital. From the policy-holders' point of view, this is an eminently undesirable arrangement. (b) If, however, the company decides to pay running expenses out of premiums (loaded to the extent necessary for that purpose), it can then organize as a participating company; and as such, it can—and, I take it, must—pay to policy-holders in dividends the whole of its annual surplus earnings, including the earnings on the endowment. But this second plan would be much more profitable to the policy-holder. True, his premiums would be greater; but this would in all probability be much more than offset by the dividends—and even by the dividends on the original capital or endowment alone. For the

loading on premiums necessary to cover legitimate running expenses of a small company such as the Teachers Insurance and Annuity Association, with almost no costs for collection, could scarcely equal the interest on $1,000,000. By the second plan, however, the policy-holder would not only participate in this interest but also in the excess earnings of the much larger sums eventually paid in by policy-holders; and would have a legal claim to such participation.

To avoid any possible misconception upon our part, however, I will put this point in the form of the two following questions, to which I trust you will favor me with specific replies at your earliest convenience:

(1) If an insurance company, organized under the laws of the State of New York, with a charter authorizing it to write participating policies, receives a certain sum, say $1,000,000, as a free gift for the benefit of its policy-holders, is there anything in the law forbidding it to pay the interest, or any part of the interest, accruing on this sum to the policy-holders, in the form of dividends or of reductions in premiums?

(2) If the answer to the preceding is in the negative, is there anything in the law which would forbid such a company to *announce* that it will pay to the policy-holders all or some specified part of the interest earned on the sum thus acquired by gift (*e. g.*, a part corresponding to the loading added to premiums to cover running expenses), it being understood that the running expenses and legal reserve have been provided for by the loading on premiums?

I note also your observations concerning the practical difficulty of establishing a new mutual company. These observations, however, manifestly have no pertinency to the case of the Teachers Insurance and Annuity Association. The difficulty you point out relates to the acquisition of a "guarantee fund" to cover preliminary expenses of organization and incorporation. The Teachers Insurance and Annuity Association was, however, provided from the outset, by gift of the Carnegie Corporation, with a fund, the interest on which was amply sufficient for all such preliminary expenses—and has, in fact, already been used for precisely those purposes. I am,

Very truly yours,

ARTHUR O. LOVEJOY.

6. *Superintendent Phillips to President Lovejoy*

June 17, 1919.

Dear Sir:

Re: Teachers Insurance and Annuity Association of America.

This will acknowledge receipt of your letter of June 12th in reference to the above Association.

The only point remaining unsettled in your mind appears to be the question as to whether it would have been feasible to successfully organize and operate the Association on a mutual plan by charging sufficiently high premium rates to enable it to comply with the requirements of §97, New York Insurance Law.

The practical difficulties in the way of successfully organizing and operating the Association on such a basis were discussed on page 3 of my letter of May 31. I do not believe there is anything further that I can add to the discussion. Further remarks would merely be the expression of my personal opinion, concerning a hypothetical situation, which I believe is unnecessary in this connection.

Replying to your specific question I beg to advise that I do not know of any provision of the law, which would prohibit a company operating on the participating plan from distributing the earnings from its capital stock and surplus to its policy-holders in the form of dividends.

In this connection, however, I would call your attention to the practical difficulties in the way of the successful operation of a company on this basis as pointed out in our letter of May 31st.

You understand, of course, that it is not a function of this Department to prescribe or dictate on what basis a company shall organize. This Department is charged only with the duty of requiring the corporation to comply with the provisions of law in the course of its organization on whatever plan its organizers may have chosen.

The responsibility for the decision to organize the Teachers Insurance and Annuity Association on a non-mutual plan rests upon the persons interested in its organization in the same manner that a decision to organize it on a mutual plan would have done.

It would, therefore, appear that my letter of May 31, 1919, contains as full a statement of the situation as I can make in all fairness to both yourself and the Association. A further expression of opinion on my part seems unnecessary.

If you have any further questions regarding the plan of operation adopted by the Association, the reasons for the adoption of such a plan or the reasons why another plan was not adopted, I would accordingly refer you to the persons interested in the organization of the Association.

Yours very truly,

JESSE S. PHILLIPS.

7. *President Lovejoy to Superintendent Phillips*

June 20, 1919.

Dear Sir:

I beg to acknowledge with thanks your letter of June 17, replying to my inquiry of June 12. Your reply satisfactorily clears up the remaining point concerning which we desired information; and shows clearly that there was no obstacle to the establishment of the Teachers Insurance and Annuity Association of America as a participating Company, through the loading of its premiums sufficiently to cover expenses, this loading being offset by distribution to policy-holders of the earnings from the capital stock given it gratuitously by the Carnegie Corporation. I am,

Very truly yours,

A. O. LOVEJOY.

III. CORRESPONDENCE WITH GEORGE RICHARDS, ESQ.

Chairman Stone to Mr. Richards

June 12, 1919.

GEORGE RICHARDS, Esq.,
141 Broadway,
New York City.

My dear Mr. Richards:

I am writing to you, as a one-time University teacher and as a recognized authority on New York Insurance Law, to enlist your interest and possible assistance in a matter which much concerns the American Association of University

Professors, and more particularly the Committee of that Association on Pensions and Insurance, of which I happen to be Chairman.

You have doubtless heard that the Carnegie Foundation, about two years ago, proposed a plan for organizing a company to insure college teachers, which finally resulted in the organization by the Carnegie Foundation of the Teachers Insurance and Annuity Association of America. The company was organized as a stock company with a total capital and surplus of $1,000,000, which was provided by the Carnegie Corporation, the purpose of the endowment being to defray initial expenses of the insurance company and to provide a surplus income sufficient to defray overhead expenses. Its charter provided that the business should be conducted without profit to stockholders, and that it should write non-participating policies.

The Committee of which I am Chairman, in a report (copy of which I enclose, if you care to examine it) criticized the organization of the new insurance company, among other grounds, for the reason that it was not authorized to write participating policies, and made no definite provision for giving its policy-holders representation in its management.

The position thus far taken by the Teachers Insurance and Annuity Association is that it cannot write participating policies or ask for a charter permitting it to write such policies for the following reasons: If organized as a participating company, it would under the New York Insurance Law be required to pay all its running expenses for each year out of premiums and assumed mortality gains. It would, consequently, in the first place be debarred from using the interest on its endowment of $1,000,000, given it by the Carnegie Corporation to pay running expenses. It would, in the second place, be compelled to load its premiums so heavily during the earlier years of the company's operation that it could not compete advantageously with established companies. Our suggestion has been that if the Teachers Insurance and Annuity Association were a participating company, it could load the premiums sufficiently to cover expenses and legal reserve but could offset this by agreeing to turn into the general surplus of the company for the benefit of the policy-holders all surplus earnings from whatever source, including interest on the endowment. What we are desirous of knowing, therefore, is whether there is any legal obstacle to such action on the part of the company, if it should be organized as a participating company.

Specifically, we desire answers to two questions:

(1) If an insurance company, organized under the laws of the State of New York, with a charter authorizing it to write participating policies, receives a certain sum, say $1,000,000, as a free gift for the benefit of its policy-holders, is there anything in the law forbidding it to pay the interest or any part of the interest accruing on this sum to the policy-holders in the form of dividends or of reductions in premiums.

(2) If the answer to the preceding is in the negative, is there anything in the law which would forbid such a company to announce that it will pay to the policy-holders all or some specified part of this interest on the sum thus acquired by gift, *e. g.*, a part corresponding to the loading added to premiums to cover running expenses, it being understood that the running expenses and legal reserve have been provided for by the loading on premiums.

In suggesting these questions, I am assuming that your familiarity with the

subject will enable you to give us your views without an extended investigation, and that you will be willing, at least in a preliminary way, to give the Committee the benefit of your views. Unfortunately, the Committee has no funds beyond a small amount for clerical expenses. If I am imposing too great a burden on you, you will, I know, tell me so without hesitation. I should hesitate to trespass on your time and attention at all, did I not consider the problem one of public interest and importance to college and university teachers throughout the country and one in the solution of which insurance men generally, and the Actuarial Society of America in particular, have been very ready to render assistance.

In behalf of the Committee, I am,

Yours respectfully,

H. F. STONE,
Chairman.

Mr. Richards to Chairman Stone

June 26, 1919.

My dear Professor Stone:

I have read your letter of the 12th inst. carefully and looked over the enclosed printed report casually, and have concluded to give you my first impression without delay.

It seems to me important that your insurance company should be a mutual company. It seems to me imperatively necessary that the policies should be participating. Bear in mind the history of life insurance companies in this state within the past few years. The situation was brought prominently before the public by a case in which we represented the plaintiff—*Greeff* v. *Equitable Life Assurance Soc.*, 40 App. Div. 180; 160 N. Y. 19; 46 L.R.A. 288; 73 Am. St. Rep. 659; N. E. 712. The charter of the Equitable provided that "each policy-holder should be credited with an equitable share of the surplus." Without any evil intent, it is natural for the management of a company to favor the treasury of the company rather than the pockets of the policy-holders, and the Equitable and other large life insurance companies in a competitive race for supremacy had got into the way of accumulating huge surpluses really at the expense and to the detriment of the policy-holders.

Our client, Mr. Greeff, on the maturity of his policy, received only a small fraction of the distributive amount of the surplus to which he was equitably entitled. The Appellate Division, with only one dissenting vote, decided that he was both legally and equitably entitled to the very much larger distributive share, but the Court of Appeals held more technically that under our statutes as they then existed he could not be permitted to maintain the action unless he could show positive fraud on the part of the directors. This he had not alleged.

The agitation of this case and of this unfortunate situation in which multitudes of policy-holders were interested gave rise to the investigation by the Committee of which Judge Charles E. Hughes was Chairman, and the remedial legislation, Law of 1906, chapter 326, followed, a conspicuous purpose of which was to give the policy-holders a more effective voice in the government of the companies and to compel the companies to make equitable distribution of surplus to the policy-holders at stated periods. This last-named provision of the statute is now embodied in section 83 of our present Insurance Law, but by its express terms it is

not applicable "to any stock life insurance corporation which . . . shall transact and shall represent itself as transacting its business exclusively upon a non-mutual basis and shall . . . issue only non-participating policies."

By making the policies non-participating, then, it would appear that the policy-holders are to be put back into the predicament in which they found themselves before this remedial legislation was enacted. I would not consent to it for one moment. I agree with you and your Committee wholly. The assets, the benefits whatever they are, must essentially belong to the policy-holders and to no one else. That we may assume to be the wish not only of your Committee, but also of the donor of the gift of a million dollars.

If it is possible to arrange for a mutual company, I agree with you that that form of organization would best fit the case. Judge Marshall has recently given a pertinent description, in an important litigation, of the essential nature of a mutual company: "As regards rights and remedies, the policy-holders are the stockholders. While the title to the property is in the company, the equitable interests therein are vested in the members. For all except corporate purposes the property of a mutual insurance company belongs to its members." *Huber* v. *Martin* (1906), 127 Wis. 412.

Likewise, the Kentucky court has recently declared that the surplus of a mutual company belongs to the policy-holders. *U. S. Life Ins. Co.* v. *Spinks*, 126 Ky. 405 (1907). But you and your Committee are altogether familiar with these propositions.

Whether the insurance company is a stock company or a mutual one, it is to be organized under the provisions of sections 70 and 71 of the New York Insurance Law. A deposit either of $100,000 or $250,000 must be made with the Superintendent of Insurance, in accordance with the provisions of section 71. I assume that it may have been the intention to deduct this amount from the principal of the gift. Perhaps it was the intention, or should be the intention, to make further encroachment upon the principal for the running expenses or some portion of the running expenses of the first year or two. I assume that the plan would be to keep the balance of the principal intact and use only the income for the benefit of the policy-holders. My suggestion is that if practicable the terms of the gift should be made to govern the disposition of the fund in general, and then as regards the insurance company the question of legality is very simple. The company merely accepts the gift. The discretionary powers granted by the donor of the gift to the company I assume would be such as the donor and the parties in interest might determine to be wise and convenient.

Responding more directly to your specific questions, I would say that I see no reason why the insurance company should not accept a gift of an endowment fund for the benefit of the policy-holders, the income from which or the income from part of which shall be paid to the policy-holders in the form of dividends or reductions in premiums, and I see no reason why the company should not announce the terms of such a gift or such features of the gift as it may choose to publish.

If I can aid you in any way, do not hesitate to call upon me.

Yours very sincerely,

GEORGE RICHARDS.

SOME FACTS ABOUT INSURANCE FOR COLLEGE TEACHERS

Mr. M. Albert Linton, Vice-President and Associate Actuary of the Provident Life and Trust Company of Philadelphia, has kindly placed the following article in the hands of the President of the Association. Mr. Linton's letter of transmission indicates the occasion and purpose of the preparation of the article. It appears to the officers of the Association to contain material which should be considered by all college teachers, especially in connection with recent publications of the Teachers Insurance and Annuity Association which have been generally distributed to the members of the profession.

August 1, 1919.

Dear Professor Lovejoy:

Some months ago you asked me whether, in view of statements by representatives of the Teachers Insurance and Annuity Association criticising my pamphlet "The Carnegie Plan of Insurance and Annuities for College Teachers," I wished to withdraw or modify any of the statements or arguments contained in the pamphlet, which had been distributed to the members of your Association by the Provident Life and Trust Company. You will recall that I answered that I did not care to make any reply to these criticisms until something official had appeared in print.

Recently there came into our hands a copy of a pamphlet published by the Carnegie Foundation entitled, "Some Misapprehensions Touching Life Insurance." As a considerable portion of the pamphlet is devoted to a discussion of the previous Provident pamphlet, I have prepared a reply entitled "Some Facts about Insurance for College Teachers," copy of which is sent you herewith. I venture to hope that this reply may be of some interest and practical use to the members of your Association and to college teachers generally, as a correction of some of the serious errors contained in the recent Carnegie pamphlet. The article is at your disposal for any use you may wish to make of it.

Our principal aim in publishing the previous pamphlet was to show that the criticism of long endowment insurance did not have a sound basis, and we attempted to set forth the facts that they might speak for themselves. The later Carnegie pamphlet repeats the same misconceptions regarding endowment insurance and further asserts that the Provident pamphlet misrepresented the situation. In the present article I have retraced the ground carefully in the hope that the intelligent reader, whatever his technical knowledge of life insurance, will not fail to get at the truth. I need hardly say that neither this article nor my previous pamphlet is intended as a competitive document to be used to obtain business for any private company at the expense of the Teachers Association. It is a comparison, on the basis of general insurance theory and experience, of the value of different types of policy, together with some comments on certain features of the

present organization and policies of the Teachers Insurance Association which I consider, and which I believe most insurance men would consider, unfavorable to the interests of the college teachers for whose benefit the company was established.

Very truly yours,

M. ALBERT LINTON.

ENDOWMENT VS. THE COMBINATION OF INSURANCE AND ANNUITY

The thought underlying the criticism of endowment insurance in the pamphlet of the Carnegie Foundation seems to be that it is too expensive for the man of limited means, that he pays for two benefits upon only one of which he can realize in the event of death, and that he can better provide against the two major contingencies of life—premature death and old age—by means of a combination of decreasing insurance and annuity contracts as offered by the Teachers Association. We are asked to believe that the combination offers a larger benefit for the same outlay on the part of the teacher. The only way to satisfy ourselves upon this point is again to analyze the two plans in detail and for the purpose of comparison we shall employ the figures on page 12 of the Provident pamphlet which refer to a $10,000 Endowment at 65 and to a $10,000 decreasing insurance policy combined with an annuity which will accumulate $10,000 at age 65.

Under the decreasing insurance-annuity combination, the total monthly premium at age 30 is $19.66, and under the Endowment at 65, $18.80. In each case the rate is that of the Teachers Association itself. Apart from any assistance rendered by the college in premium payments (which assistance could, of course, be rendered under either plan) it is obvious without further comment, that a teacher whose salary will stand a monthly premium payment of $19.66 will more readily stand one of $18.80. Or assuming that the college would contribute $5 monthly, the monthly payment of $14.66 can be less easily met than one of $13.80. The discussion should therefore be taken completely out of the realm of the teacher's *ability to pay,* and into the realm of the comparative benefits received for the two respective premiums. Table I sets forth at length the benefits payable under the two plans.

Under the insurance-annuity combination, if the insured survives 35 years, that is to age 65, the accumulated savings fund of $10,000 is available for the purchase of a life income, and the decreasing insurance policy, upon which premium payments have then ceased, has been reduced to $2500. It continues to be reduced at the rate of $300 each year until at age 70 the face value is $1000, at which amount it remains fixed. The author of the Carnegie pamphlet (p. 18) objects to the omission from the Provident pamphlet of any reference to the fact that at age 65 the decreasing insurance policy has a cash surrender value of $865. We had thought it more impressive to state (Provident pamphlet p. 6) that the policy at age 65 provided $2500 of decreasing insurance, upon which premiums had ceased, than to state that it would then be worth $865 if surrendered for cash. However, to fall in line with the suggestion of the Carnegie Foundation we shall use the cash surrender value of $865 in our present discussion.

We can therefore summarize the facts as follows: *Combination:* For the gross monthly premium of $19.66, aggregating $235.92 a year, the teacher receives protection in the event of death to the extent indicated by the series of values in column (4), averaging over the thirty-five years $11,320. If he survives to age 65,

TABLE I

Year	Teachers Association Decreasing Insurance—Deferred Annuity Combination AGE 30 Monthly Premium $19.66; Aggregating $235.92 Yearly			Teachers Association Endowment at 65 AGE 30 Monthly Premium $18.80; Aggregating $225.60 Yearly
	Insurance During Year Under Decreasing Insurance Policy	Value of Accumulated Premiums on Deferred Annuity*	Insurance Value: Total Payable to Beneficiary if Teacher Dies During Year*	Insurance Value: Total Payable to Beneficiary if Teacher Dies During Year
1	$10,000	$68	$10,068	$10,000
2	10,000	207	10,207	10,000
3	10,000	351	10,351	10,000
4	10,000	501	10,501	10,000
5	10,000	656	10,656	10,000
6	10,000	818	10,818	10,000
7	10,000	987	10,987	10,000
8	10,000	1,162	11,162	10,000
9	10,000	1,344	11,344	10,000
10	10,000	1,534	11,534	10,000
11	10,000	1,731	11,731	10,000
12	9,700	1,936	11,636	10,000
13	9,400	2,149	11,549	10,000
14	9,100	2,371	11,471	10,000
15	8,800	2,602	11,402	10,000
16	8,500	2,841	11,341	10,000
17	8,200	3,091	11,291	10,000
18	7,900	3,350	11,250	10,000
19	7,600	3,620	11,220	10,000
20	7,300	3,900	11,200	10,000
21	7,000	4,192	11,192	10,000
22	6,700	4,496	11,196	10,000
23	6,400	4,811	11,211	10,000
24	6,100	5,139	11,239	10,000
25	5,800	5,480	11,280	10,000
26	5,500	5,835	11,335	10,000
27	5,200	6,205	11,405	10,000
28	4,900	6,589	11,489	10,000
29	4,600	6,988	11,588	10,000
30	4,300	7,403	11,703	10,000
31	4,000	7,835	11,835	10,000
32	3,700	8,284	11,984	10,000
33	3,400	8,752	12,152	10,000
34	3,100	9,238	12,338	10,000
35	2,800	9,743	12,543	10,000
Average Insurance Value...			$11,320	$10,000

*Approximate Yearly Average.

the cash sum of $10,865 is available for the purchase of a life income. *Endowment at 65:* For the gross monthly premium of $18.80, aggregating $225.60 a year, he receives protection in the event of death to the extent of $10,000 and if he survives to age 65, the cash sum of $10,000 is available for the purchase of a life income.

Comparison of Net Costs

It is evident that if there is something radically wrong with the endowment principle, it might be worth investigating the combination to discover whether it is not tainted with the same error. The only difference is that the combination, with a premium of about $10 a year greater than the endowment premium, pays in the event of death, about $1320 on the average more than the endowment, and at maturity at age 65, $865 more. If this were all that should be taken into account, the combination (owing to the assumptions underlying the premium calculations and not to any intrinsic superiority) would appear to be somewhat more advantageous. In practice, however, the distribution of the surplus is a vital consideration. If the policy-holder is to receive his insurance at actual cost, the surplus must eventually be distributed; and when it is distributed, the surplus under the endowment, on account of the assumptions underlying the calculation of the Teachers Association premiums, will be larger than under the insurance-annuity combination.

For example, assuming that the surplus be distributed on the conservative assumption of 4½% interest and a mortality of 70% of the American Table, the average yearly surplus over the 35-year period will be $50 under the Carnegie combination and $61 under the Endowment at 65. The average yearly net cost—the difference between the yearly premium payment and the average yearly surplus distributed—will be approximately $186 for the combination, as compared with $165 for the endowment. The 35-year average net cost of the combination therefore exceeds the corresponding net cost of the endowment by about 12½%. On the basis of average net cost the combination is equivalent to about $11,270 of endowment insurance.

It will now be clear why in the Provident pamphlet the two plans were analyzed on pages 5 to 8, by assuming a 3½% interest rate throughout. We were discussing the scientific relationship of the endowment principle to the principle of the insurance-annuity combination. Valid comparisons must be based upon analogous fundamental assumptions. One way is to employ the method of the Provident pamphlet and assume a uniform rate of interest throughout. Another is the more complicated method of taking the published rates of the Teachers Association and computing the surplus distribution upon a uniform basis as was done in the preceding paragraph. By each method the Carnegie cost is about 12½% in excess of the endowment cost. The amount of endowment insurance equivalent over the thirty-five year period to the Carnegie combination, is $11,240 by the 3½% method, and $11,270 by the surplus method. The author of the Carnegie pamphlet takes great exception to the 3½% comparison and claims that it is unfair. On page 5 of the Provident pamphlet it is clearly stated that the assumption was made for the purpose of analysis, and on page 11 the difference between the published rates and the 3½% rates is emphasized.

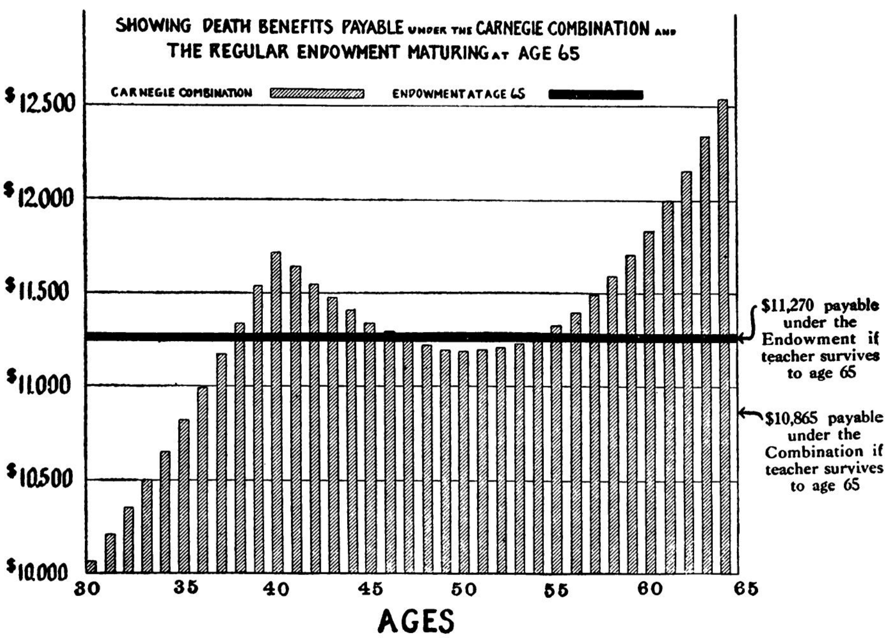
Of course, as far as the Teachers Association is concerned, we have tacitly assumed that the surplus would be equitably distributed to the policy-holders.

If the surplus were not to be distributed we could readily understand why the Carnegie Foundation would object to our comparison, since the *published gross rates* show that the Carnegie combination costs only 5% more than the endowment, and not 12½% more. We are reluctant, however, even in the face of the Charter provision that the Association will "transact its business exclusively upon a non-mutual basis," to believe that this is the explanation, since it would be a gross injustice to refuse to allow policy-holders to share in the surplus realized upon their contracts. At the same time the situation is all the more incomprehensible since the mathematical process by which it was shown in the Provident pamphlet that the cost of the Carnegie combination was relatively 12½% more than the cost of the endowment, is condemned by the Carnegie Foundation as a species of misrepresentation. Moreover the relationship between the Carnegie combination and the endowment, developed on pages 19–21 of the Carnegie pamphlet, will prove to be untrue if the contracts are allowed to share in the distribution of surplus. It is entirely understandable that the Carnegie Foundation, in its desire to avoid difficulty with the New York Insurance Law, should refrain from making any definite statement about future participation under the non-participating contracts of the Teachers Association. But it might at least avoid making statements whose validity disappears if participation be granted.

A Hybrid Endowment

Referring again to Table 1, we desire to call attention to the irregular series of values in column (4), representing the Carnegie death benefit received by the

DIAGRAM 1



beneficiary depending upon the date of death of the teacher. Now remembering that on the basis of average net cost, the Carnegie combination is equivalent to $11,270 of the endowment insurance we ask the reader to substitute $11,270 uniformly for the $10,000 in column (5). To make the situation still plainer we have prepared Diagram 1 in which the vertical shaded bars represent the series of values in Column (4). The horizontal straight line near the center of the diagram represents the uniform endowment value of $11,270.

If there be any virtue in the irregular values represented by the vertical bars, if they fit the economic needs of the average teacher better than a uniform $11,270, he should of course choose the Carnegie combination. Experience, however, has amply demonstrated that the endowment contract with its uniform amount adequately meets the needs of the average man. Moreover, it should not be forgotten that if the teacher survives to age 65—and according to modern insurance experience about 63 out of each hundred at age 30 probably will survive to age 65—the endowment will provide $11,270 instead of $10,865. Unless by some extrinsic method the hybrid endowment be made artificially more attractive than the true Endowment at 65, it is our judgment that the number of teachers who would prefer the hybrid will be exceedingly small.

The Pure Endowment Myth

And now we come to a phase of the subject which we present with apology to the non-technical reader. On page 12 of the Carnegie pamphlet we are told on the authority of the International Encyclopedia that an endowment policy is a combination of a term insurance policy payable only in the event of death during the endowment period and of a so-called "pure endowment" policy payable only to those who live to complete the endowment period. Every actuary of course recognizes this time-honored explanation which has come down from the dim insurance past when life insurance policies did not provide yearly cash surrender values. The endowment policy can be mathematically analyzed into the two types of contract mentioned; *but so can the decreasing insurance-annuity combination.* However in neither case is the explanation adequate and in this day of cash surrender and other non-forfeiture values it belongs in the category of mathematical "stunts" that may be interesting but not helpful in explaining the practical working out of things. Each of the plans is a combination of savings fund and decreasing insurance and no other analysis adequately explains either.

Perhaps, however, it will be well to substantiate the statement that the decreasing insurance-annuity combination may be mathematically analyzed into a pure endowment contract and a term insurance contract. As we are now discussing fundamental scientific relationships we shall again employ as a basis of calculation the American Table of Mortality and $3\frac{1}{2}\%$ interest, even though, in so doing, we run the risk of being misunderstood by the Carnegie Foundation. It will be recalled that by making this uniform assumption we obtain approximately the relative facts that would be disclosed if the contracts were compared upon a participating basis.

The Carnegie combination provides $10,865 at age 65 if the teacher is then living, and the annual premium for a pure endowment of this amount is $104. In the event of death under a pure endowment contract all premiums are forfeited. The term insurance contract which extends from age 30 to age 65 must provide a

series of amounts similar to the values shown in column (4) of Table I. The new series will be slightly different since we are now employing 3½% whereas the savings fund annuity of the Teachers Association employs 4%. However, referring to the short table on page 6 of the Provident pamphlet, it will be seen that the 3½% values differ but slightly from the others. Upon completing the actuarial computation it will be found that the annual premium for the term policy is $140. Adding the two amounts, $140 and $104, we obtain $244, the identical 3½% premium obtained on page 5 of the Provident pamphlet by employing the savings fund and decreasing insurance method. We have performed our "stunt" but no helpful information that would aid in explaining the Carnegie combination has been obtained. In like manner the pure endowment-term analysis is equally unsatisfactory as an explanation of the modern endowment policy. It should never have been dragged out to burden the attention of the non-technical reader.

But how shall we answer the argument on page 13 of the Carnegie pamphlet?

> "In the Teachers Insurance and Annuity Association a man of 30 can buy a $10,000 term policy ending at age 65 for a net annual premium of $122. A $10,000 endowment insurance policy will cost on the same net basis $219, both including waiver of premium in case of disability. One who bought a straight term policy and put the $97 difference into an annuity contract and who died in his sixty-fourth year would leave his dependents over $17,000 from the two benefits as compared with $10,000 from the endowment policy. The man who buys an endowment policy over a long term does so with the certainty that if he dies before its maturity he has been paying for two benefits while his beneficiaries can receive only one."

Continuing the above illustration a little further we find, if the teacher had survived to age 65, that his term policy would have expired and become worthless and that his savings fund would have amounted to about $7,550 as against $10,000 under the endowment. Incidentally at age 30 the chances of his living to age 65 were about 63 out of 100, and of dying in his sixty-fourth year, about 2 out of 100.

In order that the endowment shall not get an undue share of attention, we shall apply the above analysis to the Carnegie combination. Let the teacher take the amount of the gross premium for the Carnegie combination ($236 payable in monthly installments) and purchase, as above, a $10,000 term policy ending at age 65, putting the difference into a savings fund annuity contract. If he dies in his sixty-fourth year his beneficiary will receive about $17,700 as against $12,338 (See Table 1) under the Carnegie combination. And if he survives to age 65, the term policy will expire and the savings fund will have amounted to about $8,360 as against the $10,865 available under the combination. About all this shows is that the level term insurance-annuity combination vs. the endowment or vs. the Carnegie combination, is quite advantageous for the few who die in their sixty-fourth year, and quite disadvantageous for the many who survive to age 65. Again we express regret to the lay reader that it was necessary to lead him through a comparison of this kind.

We have now progressed far enough to see the error in the above quoted statement, that the man who buys an endowment policy and dies before the policy matures, has paid for two benefits, upon one only of which his beneficiary can realize. From the analysis in this and in the foregoing section, it is obvious that if the statement applies to the endowment it applies to the decreasing insurance-annuity combination with equal force. As a matter of fact it applies to neither.

Each is essentially a combination of savings fund and decreasing term insurance. When a death occurs, the amount paid to the beneficiary is in each case made up of the then amount of the savings fund accumulation and the then amount of the decreasing term insurance. Under each plan the man pays for two benefits and, in the event of death, his beneficiary realizes on both.

Term Insurance

On page 24 of the Carnegie pamphlet the writer discovers the real reason why in its pamphlet the Provident Life and Trust Company does not recommend the combination of term insurance and deferred annuity to its own policy-holders. He announces seriously that the Company cannot afford to do so for the reason that its agents could not make a living by selling term insurance. We almost despair of the ability of the Carnegie Foundation to grasp the essential fact that the endowment policy involves both a term insurance and a savings fund element. One glance at Diagram 1 of this article will clearly indicate why we prefer the true endowment to the hybrid. To us the level black line of the endowment, supported by our half century's experience with its simplicity and adaptability, is greatly to be preferred to the curious peaks and hollows of the hybrid.

Now a word as to straight term insurance, which is sometimes considered by theorists to be the most advantageous form of insurance for the average man. They may even go so far as to charge that the companies withhold term insurance from the public for the reason that their agents could not make a living by selling it. In the first place if term insurance were most advantageous for the insured, the companies would encourage the extensive sale of term insurance and it would be sold in a manner to yield the agent a living. As a matter of fact, straight term insurance, as its name indicates, is valuable for temporary purposes only and has limited application. The man who carries a regular term policy to age 65 and then sees it expire is likely to denounce the company which collected his premiums all those years and then at the end gave nothing back. It is hard for him to realize that he has simply paid for the temporary protection, just as he has paid for his fire insurance protection, and that he should expect nothing more than he expects upon the expiry of his fire insurance policy, under which no fire has occurred. As a matter of fact, he becomes a disgruntled policy-holder whom mathematical arguments seldom satisfy.

On the other hand when the decreasing term insurance principle is combined with the savings fund principle, as in the old age endowment policy, we attain an ideal combination. We all recognize the vital importance of providing against dependence in old age. This the savings fund principle can accomplish. But it falls down in the event of premature death. Hence the logical addition of the safety device in the form of decreasing term insurance that *automatically* reduces as the savings fund increases. Nothing could be simpler than this combination or more serviceable to the insured. And if theorists believe that term insurance without the savings fund accompaniment provided in the endowment policy, is more advantageous to the insured and is being withheld from the public because, for selfish reasons, life insurance companies and their agents refuse to sell term insurance, about all we can say is that practical insurance experience will in due course bring them to another point of view.

It is amazing that the Carnegie Foundation has failed to grasp the wonderful simplicity of the endowment principle. A man in his early years, say at age 30, looks forward to the close of his income earning career and desires to make provision against the dependency of old age. He sets his mind upon accumulating, say $10,000 at age 65, and finds that he can accomplish his purpose by a yearly payment of $145, assuming 3½% interest. The only difficulty is that death may intervene and cut short the well laid plans so that his wife and children will be plunged into privation and suffering. He finds, however, that for $74 more, or $219 in all, the Teachers Association will promise to pay immediately at death, the same amount which would have been paid at 65, if he had lived to complete his plans. The $74 (omitting reference to the small amount charged for the disability feature) provides for automatically decreasing term insurance of such a character that in any year its amount is exactly the amount by which the accumulated savings fund falls short of $10,000. Nothing could be simpler in its results than this single contract automatically performing its double function and some day the Teachers Association will come to realize its inestimable value.

Separation Into Two Contracts

It should be emphasized again that we are interested in the comparison between the Carnegie Company's combination and its Endowment at 65, primarily to show that the endowment is ideally adapted to protect against the contingencies of death and old age, and that the separation into two contracts, one decreasing insurance and the other savings fund annuity, does not lower the cost of the benefits conferred. If other considerations render it advisable to separate the contracts in the case of teachers, then the objections to the endowment principle, as such, are wholly extrinsic. This is clearly indicated on pages 14 and 15 of the Provident pamphlet. We will now take up the specific reasons for the separation into two contracts outlined on pages 22 and 23 of the Carnegie pamphlet.

> 1. "The man who buys endowment insurance is certain to pay more for his protection than the risk is worth if he dies before the completion of the endowment period, since he pays for two benefits and can realize only on one."

We have shown that if the statement applied to the endowment, it would apply also to the Carnegie combination. As a matter of fact, as we have seen, it applies to neither.

> 2. "Under the law the maximum rate of interest on an insurance contract is 3½%, while the deferred annuity contract may be on a 4% basis. The teacher thus obtains a larger guaranteed result for his deferred annuity contract by having it separate."

In any company in which the surplus is distributed, the larger guarantee under the deferred annuity will have no practical value. The net cost under participating contracts depends upon the actual experience, not upon the assumptions underlying the premium calculations.

> 3. "To take out an insurance policy requires a medical examination, to take out a deferred annuity contract requires no medical examination."

Let us take the case of a teacher with a family. The Carnegie plan contemplates that he will take out both a decreasing insurance policy and a deferred annuity. If he is in bad health he will be able to obtain merely the annuity, and the insurance protection will have to be foregone. If the endowment were the standard, he would also be limited to the annuity and would have to forego the insurance protection. In this respect the two plans are exactly alike.

> 4. "Under an endowment policy covering a long term the proportions of insurance and investment are arbitrarily fixed. In most cases a teacher will desire to change his proportion of insurance to annuity accumulation as his age and financial circumstances change. For example, with increasing salary he will increase his annuity accumulation, or, on the other hand, in case of disability he will desire to avail of his annuity at an earlier age but to continue with his insurance. Under an endowment insurance policy it is not possible to provide these variations which the teacher is certain to desire and which it is the object of the Teachers Insurance Association to provide."

In our judgment all of the necessary variations and combinations could be attained by offering (1) the old age endowment, (2) the savings fund annuity, and (3) short term insurance, as indicated on pages 14 and 15 of the Provident pamphlet.

> 5. "No life insurance company can under the New York law issue an endowment policy guaranteeing that the proceeds may be invested in any life annuity upon terms as favorable as the Association's rates based upon the McClintock Table with 4% interest."

The Teachers Association advertises that annuitants may purchase annuities at McClintock's 4% rates. We know of nothing in the New York law to prevent the Association from providing that the proceeds of their life or endowment policies may be applied to purchase immediate annuities at the same rates.

> 6. "Colleges recognize their obligation to join with their teachers in contributions to a deferred annuity policy, but for obvious reasons they do not contribute toward the premiums of insurance policies."

Under the endowment policy, a college can contribute toward the savings fund element in the endowment premium, thus allowing the teacher to pay the full premium for the insurance element.

Mutualization

The question of making the policies of the Teachers Association participating is discussed on pages 26 to 39 of the Carnegie pamphlet. We confess that we are glad to note in the later pamphlet the absence of the statement in the Twelfth Annual Report of the Carnegie Foundation (p. 46) that during the early years the surplus if distributed in annual dividends would not in some cases pay the cost of postage. We are now told, first, that it is practically impossible to start a new insurance company under the New York State laws, and second, that it was found entirely in the interest of future policy-holders to incorporate the Teachers Association as a stock company with non-participating policies!

As to the first reason, I am unconvinced. The Teachers Association is dealing with a homogeneous, well organized clientèle and will not employ agents. It is the extremely heavy expense of building an agency organization that renders it practically impossible for a new commercial company to comply with the expense limitation of the law. It is true that if the policies were issued on the participating

plan, the premium rates of the Teachers Association should be increased by the addition of what is termed an "expense loading." But the ultimate net cost would not be changed, as the loading, with a year's interest, could be returned each year in the distribution of surplus. If with properly loaded premium rates the Teachers Association still doubted its ability to organize under the New York law, it could have incorporated in any one of the adjoining states and then have entered New York a year or so later, when certainly it should have been able to comply with the provisions of Section 97 of the New York law.

As to the second reason, I am also unconvinced. A contractual right to receive surplus certainly gives the policy-holder an opportunity to have more voice in the disposition of the surplus than the absence of a contractual right. The teachers comprise a homogeneous group with good facilities for intercommunication. In case of a difference of opinion between them and the Teachers Association as to the manner and amount of the surplus distribution, the contract right would add greatly to the teachers' ability to make their influence felt. Personally, I would be willing to sacrifice a good deal to obtain a participating contract.

Conclusion

Finally we would again repeat the statement that the Provident, and in so far as we are aware, other private life insurance companies will not attempt to stand in the way of the progress of the Teachers Association. We realize fully that by virtue of the expense subsidy, the net cost in the Teachers Association will be low if the policies are allowed to participate in the surplus. It would be exceedingly short sighted in us to represent that our insurance would be cheaper than participating insurance enjoying so large a subsidy. We wish the Association success, knowing full well that the establishment of a sound system among a group so influential as is the group of American college teachers, will greatly benefit the business of insurance as a whole.

The two concrete suggestions that we make are that the Teachers Association adopt its Endowment at 65 as the standard policy for teachers with dependents, and that steps be taken to place the Association upon a mutual basis so that the teacher will have a contractual claim upon the surplus.

M. Albert Linton.

OUTLINE OF A CONTRIBUTORY RETIRING-ALLOWANCE PLAN

[The following paper, contributed by Professor Theodore de Laguna of Bryn Mawr College seems to the Chairman of Committee P to contain information and suggestions which should be laid before the members of the Association.]

It is safe to say that, for the most part, boards of trustees will not be anxious to drive faculties into the acceptance of the Carnegie pension plan, if they can be shown an alternative plan that is more advantageous from a purely financial point of view. Such a plan is briefly indicated by Professor Lovejoy and Professor Stone in the following terms: "The [non-contractual] offer [by the Carnegie Foundation] of an additional half per cent interest on the accumulated sums paid by teachers and institutions toward teachers' annuities brings the total rate of interest on these payments to less than the rate obtainable from government bonds or good municipal bonds—the purchase of which would be a much more advantageous means of accumulating the amount necessary for the eventual purchase of an annuity."

The following pages will be devoted to a defense and an elaboration of this suggestion:

I. The suggestion has been criticised on the ground that no allowance is made for the cost of administration of a pension fund to be established by the particular college for its own teachers. Granted that the trustees of the college contribute *gratis* their expert services in the purchase of securities, one or more clerks will be needed to keep track of the returns from the investments and the crediting of each teacher with his proper share in the returns; and these clerks must be paid.

This objection is formally sound. The portion of a sentence which I have quoted does *not* contain a reference to clerical salaries. But neither does it contain a reference to the three considerable deductions that must be made from the Carnegie offer of 4½ per cent interest: (1) for the absence of option in the method of paying accumulations at death; (2) for the narrow limitation of options at retirement; (3) for the hazard of being in impaired health when the annuity is purchased. Let us briefly consider these three points.

(1) The Carnegie plan provides that in the event of the death of

the teacher prior to retirement, the accumulated sum is to be paid to his estate in 120 monthly installments, with interest continuing at 4 per cent.

Let us suppose that the teacher dies at age 55. In the typical case which is outlined in the Carnegie Hand Book, the accumulated savings amount to $10,219, and the heirs receive monthly payments of $102.80. As the teacher's salary has recently been $250 a month, this is likely to appear a meager monthly income: and the whole, or almost the whole of it, is only too likely to be spent each month. But it is not income. At the end of 10 years, the widow and perhaps a half-educated child (for late marriage of college teachers is not rare) may find themselves on the verge of destitution.

Even if the widow has the forethought and courage to economize, the money comes to her in an inconvenient way for the purpose of investment; and no provision is made for any assistance to her in the matter of investment.

The intent of the provision is plain. In the first place, by preventing sudden calls for large sums of money, it facilitates the investment of funds by the annuity company, and makes possible the earning of a slightly higher interest-rate. But the heirs pay dearly for this; and almost the same benefit could be secured if the monthly payments were made for one year, and the whole balance were paid over at the end of that time.

In the second place, the provision is intended to prevent the rapid squandering of the money by a widow or other heir, who has no business experience. But the result is to make the squandering of the money less rapid, indeed, but doubly probable.

The whole sum ought at the earliest practicable moment to be available for reinvestment. But, for the reason just given, either the investment of the money ought to be in the hands of a trustee, or (if that is not feasible) some one should have been appointed by the College to act with her in an advisory capacity. What investment should be made would depend on many circumstances. Ten thousand dollars is not a great sum; but with the advice of a good business man the widow might do something with it. If she were alone in the world she might buy a meager annuity. The adviser might recommend a selection of conservative stocks; or, if the woman's immediate needs were great, he might recommend less conservative stocks, paying seven or eight per cent. She might open a boarding-house or a small school, risking only a part of her

capital in this way. All would depend on the extent of her ability and of her needs. Any course, almost, would be better than letting the money slip away in driblets, never to return.

It must be remembered, too, that even if the accumulated sum is only $1,000, or only a few hundred dollars, the prescribed mode of payment is the same. There is no option whatsoever.

How far this provision operates to the prejudice of the interest-rate allowed on deposits, cannot be closely estimated. There is, however, this pertinent reflection to be made. If it were possible for the heirs to secure the money from some quarter at once by the payment of a discount, they could hardly expect this discount to be calculated on a basis of less than 5½ per cent interest; and that would involve a loss of about six per cent of the whole sum. On contributions made through a period of 20 years this would amount to an interest-reduction of almost one-half of one per cent.

(2) The annuity-rates offered under the Carnegie plan are, considered by themselves, very good. But not every man at 65 is in such circumstances as to make an annuity a desirable investment for him. He can, indeed, in that way secure the largest possible income for himself for the remainder of his life. But there may be other considerations. And no reasonable man would voluntarily commit himself at 30 to making such an investment at 65.

It may be replied that if the annuity is bought for him he anyhow gets his money's worth. He does—if an annuity is what he desires; otherwise not. The annuity is calculated on a 4 per cent basis (this is unaffected by the supplementary offer of the Carnegie Foundation); and a more liberal rate could hardly be promised by an annuity company. But if the man does not need and does not want an annuity, he is simply compelled to forego any higher return. If he were a free agent, he might, say, put his money into preferred stocks paying 6 per cent interest. That would be little more than half of the annuity; but it might be sufficient for his needs, and it would leave the property intact for his children.

This loss of freedom, attaching to savings over a period of 30 years or more, is a decided detriment to the interest-rate. I doubt whether any good business man would estimate it at less than a quarter of one per cent.

(3) The case is more serious when the teacher, at the age of retirement, is in seriously impaired health, or when he is forced by ill

health to retire at an earlier age. Here he suffers a loss which approximates 18 per cent of the accumulated sum.

It will be recalled that at retirement the teacher must choose between three different forms of annuity, referred to as Options I, III, and IV (Option II is postponement of the retiring-age). The three forms are as follows:

I. A straight annuity, terminating at the teacher's death.

III. An annuity considerably less than the above, with the proviso that after the teacher's death half of the annuity will be continued to his wife, if she survives him.

IV. An arrangement whereby the whole sum, without further interest, will be paid to the teacher or his heirs in 128 monthly installments; and, in return for the sacrifice of interest, the teacher will, if he lives for more than ten years and eight months, receive equal monthly payments until his death. Each installment is, again, considerably less than the monthly income under Option I.

Now the teacher who is in ill health may find himself in a serious quandary. If he is alone in the world, it matters little; but if he has dependents the great problem must be for him to secure what he can for them. Option I is out of the question. He may live for years, but he cannot count on doing so. If he has a wife, Option III will give her an annuity equivalent to about one-half of the accumulated savings. Option IV will save a little more than four-fifths of his money. But every way he stands to lose.

The heart of the matter is this. For a man in sound health, Option IV is fair. The sacrifice of interest is balanced by the possibility that he will live beyond the final payment of the principal. But for the man in broken health, though this possibility almost always in some slight degree remains, it does not balance the loss of interest. Even the extreme case, where the teacher finds himself with his days numbered by an incurable disease, must be expected to occur occasionally; and his family have no escape from loss—unless he is rich enough to be able to postpone his annuity indefinitely (under Option II). Then at his death, his family get the whole sum in the usual 120 monthly installments.

The inequity of this case attaches in some degree to the conditions under which every teacher is asked to begin his regular payments into the annuity fund. For every teacher must face the possibility of being compelled to retire by serious ill

health, or of being in impaired health at the regular age of retirement.*

The question may be asked whether some allowance is not made for this possibility in the annuity rates. The answer is in the negative. The rates are exactly the same as those offered to voluntary purchasers, whose funds have been accumulated elsewhere.

The amount of the loss, under Option IV, is 18 per cent at the maximum; from which must be subtracted the amounts paid to those men who, in spite of their ill health, continue to live for more than ten years and eight months (under Option IV); and to which must be added the amount lost to the estates of men who, in spite of ill health, choose Option I and die in a relatively short time.

The important question for us is: How much is the interest-rate diminished by the hazard of being compelled to buy an annuity when in impaired health? A few of the relevant facts are as follows:

Not more than 20 per cent of the men who reach the age of 65 are considered to be fair risks for new life insurance. In the favorable occupation of college-teaching, the proportion does not exceed 25 per cent.

No medical examination is required at the purchase of annuities. But it is not usual for men in serious ill health to buy annuities. And, as a matter of experience, voluntary annuitants actually live for about the term of years that is expected of those who are insurable.

The significance of these figures should not be exaggerated. On the one hand, medical examiners must of necessity err on the safe side. The life insurance companies can better afford to refuse sound business than to be loaded up with unsound business. On the other hand, the long life of voluntary annuitants is not entirely due to self-selection. Something must be ascribed to the assurance of support given by the annuity itself.

As a rough estimate, I should say that a savings-fund, whose depositors are subject to this hazard, is practically allowing an interest-rate that is about one-half of one per cent below the ostensible rate. It may well be that the average loss is less than this; but, on the other hand, the insecurity itself is a detriment; and, in an important class of cases, the loss is suffered by those who are least

* The compulsory purchase of annuities is almost as unjust to the purchaser as the compulsory sale of life insurance to all comers would be to the insurance company.

able to bear it—namely those who are compelled by ill health to retire at an early age. I am inclined to think that a man of good business judgment would generally prefer the purchase of a selection of bonds paying 4 per cent interest, to the depositing of money in this savings fund at 4½ per cent, with the chance of losing 18 per cent of the accumulated sum.*

On the whole, when all these sources of loss are considered, it must, I believe, be granted that the total prejudice to the interest-rate is easily in excess of one-half of one per cent. We may therefore fairly assume it to be not less than that amount.

II. Against the proposition that the colleges should set up their own pension-funds it is urged that no college can sell annuities to its teachers without a special charter; and that, given this charter, a college would have to set aside a disproportionately large capital as the basis of its small annuity business.

But no one proposes that the colleges should go into the annuity business. Several of the existing companies offer rates upon which they could hardly hope to improve. It is only suggested that a college may well establish its own savings-fund for the eventual provision of retiring allowances—either through the purchase of annuities or otherwise, as the health and circumstances of the particular teacher may indicate.

The suggestion has, indeed, been made that the college teachers of the country should organize an association for the sale of both annuities and life insurance. Such a plan offers certain advantages, which have often been pointed out. But it would require a considerable capital; and, especially in the earlier years of the association, it would involve a serious risk. There is certainly no immediate necessity for the venture.

There is also the possibility of establishing a teachers' savings-fund under the auspices of the American Association of University Professors. Such an institution would need no capital. It would guarantee nothing, but would simply allow depositors the interest actually earned. If deposits were withdrawable only at death or on retirement from the profession, and if a year's notice were required—

* In defense of the Carnegie plan it is urged that it would not be feasible for any company to sell annuities to the sick at preferential rates. That is probably true. The danger from fraud would be too great, since many forms of disease can be feigned with great exactness. But the defense is misdirected. The inequity is, not that the sick are not given preferential rates, but that they are forced to buy annuities at all.

except as it might suit the convenience of the institution to waive this requirement—a much higher interest could be secured than by ordinary savings banks. There is no inherent impossibility in the scheme. But it has no evident superiority to the institution of separate savings-funds for the different colleges. It might, perhaps, facilitate the movement of teachers from one institution to another. But the separate funds have the decided advantage of being more easily established.

In the outline of a pension-plan given below, it is assumed that the relations between faculty and trustees are of such a character that the members of the faculty are willing to repose a certain degree of trust in the integrity and sense of honor of the trustees. This is almost universally the case. Where it is not the case, a special board of managers, in which the faculty are adequately represented, must be instituted to take control of the savings-fund.

Outline of a Retirement Plan for Colleges

Section I. The trustees of the college shall offer to retain for investment 5 per cent of the salary of any member of the faculty; exception being made (1) of one-year appointees, (2) of instructors who are less than 30 years of age and who have been less than three years in the service of the college, (3) instructors who are more than 55 years of age, and (4) instructors for whom a retiring allowance has already been provided.

Section II. The trustees shall further offer to duplicate each sum thus retained; the joint amount to be eventually used to provide a retiring-allowance for the instructor, either by the purchase of an annuity or in any other way that his health and circumstances may make advisable.

Section III. The trustees shall engage the college contractually to pay the retiring instructors twice the amount retained from their salaries for that purpose, with interest at a rate that the college will with practical certainty be able to secure.

Section IV. The trustees shall declare their intention of allowing whatever interest, up to 4 per cent *per annum*, compounded annually, the funds may actually earn.

Section V. Any sum earned in excess of 4 per cent interest shall be allowed to accumulate, in order to be used by the trustees, with the advice of a committee of the faculty, to supplement the allow-

ances of instructors who may be forced to retire prematurely, or for the relief of instructors who may be temporarily disabled.

Instead of the last two sections, it might be provided simply that the trustees shall declare their intention of allowing whatever interest the fund actually earns. This would very likely be about four and one-half per cent. But 4 per cent is as much as the nominal 4½ per cent promised by the sponsors of the Carnegie plan is really worth; 4 per cent will normally provide a sufficient retiring allowance; and the reservation of the balance for the benefit of the sick will amply provide for the exceptional unfortunate cases.

Section VI. In the case of instructors who are between the ages of 41 and 55 years, the trustees shall offer to duplicate contributions in excess of 5 per cent of the salary, up to the amount necessary, with interest at 4 per cent, compounded annually, to produce at age 65 the sum of [say] $15,000.

Fifteen thousand dollars will, at age 65, buy an annuity amounting to a monthly income of about $140 ($125 for a woman). To produce this sum, the annual contribution from an instructor at age 41 would be about $165. In the case of an instructor 55 years of age it would be a little over six hundred dollars. Beyond that age a contributory retiring-allowance plan is hardly practicable.

Section VII. In the event of the death, resignation, dismissal, or failure of reappointment of an instructor prior to retirement, the trustees shall, at their convenience but within one year, pay to him or to his heirs the amount standing to his credit; that is to say, his own contributions and those of the college in his behalf, with interest at the earned rate (up to 4 per cent, compounded annually).

Section VIII. The investment of the sum standing to the credit of a retiring instructor shall be made by him with the assistance of a financial advisor appointed by the trustees; and the services of this advisor shall also be available for the heirs of an instructor who shall die while in the employ of the college.

The retiring instructor knows best his own needs and those of his family. The advisor appointed by the trustees can, in general, be counted on to know far more about the safety and productivity of investments. The investment of the sum ought to be in the instructor's hands, for it is his deferred salary. But the college has a moral interest in the matter; and with this interest goes a certain moral right. It should therefore be understood that the instructor will on no account disregard an unfavorable judgment of the advisor.

Section IX. In the case of instructors who are over 55 years of age, the trustees shall make such provision as the occasion may require.